5 November 2020

Press release

Incorrect data and false conclusions: PensionsEurope corrects Better Finance report on Bulgarian pension funds

On 24 September 2020, Better Finance published the eighth edition of its report on the Real Return of Long-Term and Pension Savings which aims to show the real returns of pension savings in various countries from the last 20 years. Together with our Bulgarian Member Association BASPSC (Bulgarian Association of Supplementary Pension Security Companies), PensionsEurope has thoroughly analysed the country profile of Bulgaria[1] and concluded that it is incorrect. Based on incorrect data Better Finance draws wrong conclusions and declares that Bulgarian private pensions have failed. The report goes as far as to recommend reversing the contributions to the State pension fund in the future (starting e.g. in 2022) and calling for a transfer of the existing pension savings to the Government fund.

Matti Leppälä, CEO/Secretary General of PensionsEurope, said:
"*The old-age dependency ratio in Bulgaria projected to be 55% by 2050, which means that there will be less than two persons in working life for every retiree, and this is one of the most difficult projections of the countries covered in the report. It is thus clear that in Bulgaria the PAYG social security pension system will be very challenged and funded supplementary pensions are increasingly necessary in order to achieve adequate and sustainable pensions."*

"The country profile of Bulgaria contains several incorrect numbers and calculations – most importantly an incorrect rate of returns for the Bulgarian pension funds. The Better Finance report also includes wrong information on Bulgaria in general. For instance, the report incorrectly states that "in Bulgaria, data for Professional Pension Funds (pillar II and III) is no longer available since 2018", while the Bulgarian Local Regulator i.e. Financial Supervision Commission provides on a quarterly basis full disclosure on pension market development by type of funds and players with the same quality and quantity of information."

In its policy recommendations regarding Bulgaria, Better Finance recommends reversing the private pension reform of 2000, and this in fact would mean nationalising individual pension savings in Bulgaria. PensionsEurope warns that Better Finance's recommendation would be detrimental to Bulgarian pensions. In 2021, Bulgaria is entering the pay-out-phase from private pensions and policy recommendations to dismantle the existing system are harmful.

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[1] See Annex. Other country profiles PensionsEurope has not yet had time to analyse in depth, but we are aware that at least some of them contain mistakes and are incorrect as well.

Mr Leppälä continues:

"Based on incorrect information, Better Finance's recommendation to reverse private pension contributions and transfer savings to the Government is dangerous. This recommendation is also very much in contradiction with the numerous European policy recommendations, latest the Capital Markets Union New Action Plan in September 2020, highlighting the importance of strengthening supplementary pensions in order for all Europeans to have adequate and sustainable income in old age."

"There is also clear inconsistency in Better Finance's messages. In its press release "Dismantling the Estonian Pension System is not the Answer" (of 27 October 2020), Better Finance correctly calls to reverse the decision to dismantle the foundation of the second (occupational) pillar of the Estonian pension system. If Better Finance calls not to sacrifice the long-term and pension adequacy in Estonia, why is it ready to do so in Bulgaria?"

In general, PensionsEurope welcomes research on the quality of occupational and personal pensions and the outcome of pension savings, and we also strongly support consumer rights. Together with our Member Associations, PensionsEurope is willing and ready to further co-operate with Better Finance to improve the methodology and quality of its reports. Ensuring quality is crucial also for the fact that nearly 60 % of the annual income of Better Finance comes from the EU i.e. the European taxpayers.

About PensionsEurope

PensionsEurope represents national associations of pension funds and similar institutions for workplace and other funded pensions. Some members operate purely individual pension schemes. PensionsEurope has **24 member associations** in 17 EU Member States and 4 other European countries[2].

PensionsEurope member organisations cover different types of workplace pensions for over **110 million people.** Through its Member Associations PensionsEurope represents more than **€ 4 trillion of assets** managed for future pension payments. In addition, many members of PensionsEurope also cover personal pensions, which are connected with an employment relation.

PensionsEurope also has **26 Corporate and Supporter Members** which are various service providers and stakeholders that work with IORPs.

PensionsEurope has established a **Central & Eastern European Countries Forum (CEEC Forum)** to discuss issues common to pension systems in that region.

PensionsEurope has established a **Multinational Advisory Group (MAG)** which delivers advice on pension issues to PensionsEurope. It provides a collective voice and information sharing for the expertise and opinions of multinationals.

What PensionsEurope stands for

- A regulatory environment encouraging workplace pension membership;
- Ensure that more and more Europeans can benefit from an adequate income in retirement;
- Policies which will enable sufficient contributions and good returns.

Our members offer

- Economies of scale in governance, administration and asset management;
- Risk pooling and often intergenerational risk-sharing;
- Often “not-for-profit” and some/all of the costs are borne by the employer;
- Members of workplace pension schemes often benefit from a contribution paid by the employer;
- Wide-scale coverage due to mandatory participation, sector-wide participation based on collective agreements and soft-compulsion elements such as auto-enrolment;
- Good governance and alignment of interest due to participation of the main stakeholders.

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[2] EU Member States: Austria, Belgium, Bulgaria, Croatia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Netherlands, Portugal, Romania, Spain, Sweden. Non-EU Member States: Iceland, Norway, Switzerland, UK.

Annex: Bulgarian Association of Supplementary Pension Security Companies comments on Better Finance report regarding Bulgaria

BASPSC

BULGARIAN ASSOCIATION OF SUPPLEMENTARY PENSION SECURITY COMPANIES

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Comments on Better Finance report regarding Bulgaria

Referrals to the general document:

(1) The report compares different countries, but the calculated returns are not comparable because of the application of different methodologies. Part of the returns figures are calculated as Money-Weighted Returns, while the others are calculated as Time-Weighted Returns and the third figures are actually calculated using the formula Yield =Return as % of AUM.

Besides, the figures for Bulgaria on page 17 and page 18 are not correct and lead to wrong analysis and judgment.

The **correct figures** should be as follows:

	Aggregate summary Average real net returns in different periods		Pillar II- Occupational pensions						
	1 year		**3years**		**7 years**		**10 years**		**Max availabl e**
	2019	**2018**	**2017-2019**	**2016-2018**	**2013-2019**	**2012-2018**	**2010-2019**	**2009-2018**	
Bulgaria	2.6%	-6.7%	-0.3%	-0.2%	1.8%	1.8%	1.6%	1.5%	0.9%

	Aggregate summary Average real net returns in different periods		Pillar III- Voluntary/individual pensions						
	1 year		**3years**		**7 years**		**10 years**		**Max availabl e**
	2019	**2018**	**2017-2019**	**2016-2018**	**2013-2019**	**2012-2018**	**2010-2019**	**2009-2018**	
Bulgaria	3.1%	-7.2%	0.0%	0.5%	2.8%	3.0%	2.3%	2.4%	0.0%

Source: FSC, NSI, BASPSC

(2) The statement on page 39 about insufficient information for PPFs since 2018 provides some alarming conclusion that the Regulator used to disclose some information in the past which is no longer available (hidden from the clients and public). See www.fsc.bg Statistics.

(3) Nevertheless, the general conclusion is that the transparency of cost disclosures is not improving (page 39) and the author does not comment this particularly for Bulgaria where a huge step has been undertaken toward to a much higher transparency, minimum data requirements for disclosure and provision of annual statements to the members have been introduced to include detailed information regarding all fees and taxes, etc. (See Ordinance

56 on Investment policy and Ordinance 61 on Information and web page minimum requirements to be disclosed to the insured people.

(4) In table GR10 (B) – page 49, the data for the inflation in non-Eurozone member states is comparable across the countries for the years between 2000 and 2017 as the Eurostat annual data (average index and rate of change - PRC_HICP_AIND) is used. The only exception is Croatia where between 2000 and 2014 when a different statistical data is used. For the years 2018 and **2019 different statistical data has been** used for all the countries which makes the comparison with the prior years (2000 - 2017) completely matchless which at the end results in misleading conclusions. Especially for Bulgaria, data for 2018 and 2019 are not correct.

(5) Data for pension funds' portfolios (presented on page 52) for Y2019 and Y2018 does not correspond with the actual ones. (*See* www.fsc.bg *Statistics*)

(6) Disclosed rate of returns for all countries (page 67) are not comparable because figures are disclosed for different periods and different methodologies;

(7) Disclosed rate of returns for pension funds in Bulgaria (page 67 and page 68) for the periods 2002-2017; 2002-2018 and 2002-2019 are not correct.

Correct Figures should read as follows:

Real Net Return	**16 years (2002-2017)**	**17 years (2002-2018)**	**18 years (2002-2019)**
Pillar II- Occupational pensions	1.94%	0.56%	0.85%
Pillar III- Voluntary/individual pensions	0.43%	-0.27%	0.01%

Source: FSC, NSI, BASPSC

Referrals to Country review Bulgaria:

(8) Rates of return on page 118 do not reconcile with the ones presented on page 17 and 18.

(9) The author provides very simplistic approach to compare and back-test the performance of the funded pension funds in Bulgaria with his own constructed benchmark. Such an approach is not applicable in Bulgarian case due to legislation provision for minimum rate of return calculated on a 24 months basis which is obligatory to be disclosed quarterly by the regulator: FSC. Penalties for performance below such a benchmark are severe and passive investment portfolio like the one suggested may result in tens of millions EUR payments due by the pension provider in certain cases. Even excluding the remark above and without contesting the author's right to offer and create synthetic products and portfolios, **at least two major weaknesses and erroneous conclusions should be noted in this case:**

- In general, every back-testing has a huge problem - it is normally designed as of today on the basis of past time and a clear result, and you can always select assets and ratios to show a desired result (common practice of investment bankers in creating and marketing of their next financial engineering product), but these rather theoretical benchmark portfolios do not guarantee better performance in the future.

  Although the author handles financial economic terms and concepts well, he also fails to quantify and present properly the risk of the benchmark portfolio. Applying a well-established and widely recognized methodology applicable for the portfolio risk, namely "Standard Deviation of the portfolio" and "Sharp ratio" for that same period of 16-years, it appears that the benchmark portfolio is characterized by **significantly higher volatility m**easured through the standard deviation. At the same time the "Sharp ratio" (yield achieved per unit of risk) of the PF, although not much higher than the one recorded for the indicative benchmark, but it is still obvious that **the Sharpe ratio of the fictitious benchmark is lower than the ratio's levels derived for the VPF and PPF**. This means, in practice, that the reasoning for the lower risk of the benchmark portfolio is **misleading and not true,** both, on the one hand based on the volatility (standard deviation) and on the basis of the synthetic risk indicator – "Sharp ratio".

	VPF	**PPF**	**GPF**	**Portfolio Benchmark**
Standard deviation	3,82	2,89	3,16	5,22
Sharpe coefficient	0,72%	0,74%	0,76%	0,69%

(10) Cited on page 121 the Average replacement ratio of 37% sourced by Eurostat is frustratingly lower than the one presented on page 29 sourced by OECD, namely: 89%. The figure should be further reconciled and corrected.

(11) Calculated time-weighted returns figures on page 122 are not correct.

Correct Figures are as follows:

Table BG2. Annualized Time-Weighted Returns							
	Universal pension funds				Voluntary pension funds		
Holding Period	Gross Return	Nominal Net Return	Real Net Return	Holding Period	Gross Return	Nominal Net Return	Real Net Return
1 year (2019)	7.63%	6.45%	3.35%	1 year (2019)	7.19%	6.26%	3.16%
3 years (2017-2019)	3.94%	2.68%	0.28%	3 years (2017-2019)	4.19%	3.41%	1.01%
7 years (2013-2019)	4.87%	3.36%	2.95%	7 years (2013-2019)	5.31%	4.50%	4.09%
10 years (2010-2019)	5.20%	3.51%	2.30%	10 years (2010-2019)	5.35%	4.54%	3.33%
Since Inception	7.59%	4.56%	1.55%	18 years (2001-2019)	6.13%	4.73%	1.48%

Sourse: Bulgarian FSC , HICP- Bulgarian Statistical Institure (NSI)

(12) On page 128 the author misleadingly provides data for pension funds fee levied on transfer between funds. Such a fee is no longer legally possible to be levied since August 2015 (see State Gazette 61/2015) when new amendments to the in the Social Insurance Code: article 202 have been introduced.

(13) Calculations presented by the author on page 130 do not recognize and do not include **sizeable cumulative outflows of payments on behalf of the PF** over the years directed to the SSS (State Security Institute) and the state Silver Fund (amounting to c. 200 million EUR until 2019) that artificially understates substantially the results for the respective returns.

Correct Figures taking into account the above outflows for the same period under observation are as follows:

Table BG7. Universal Pension Funds (UPF) Money-Weighted Returns					
	Nominal Returns (Gross of fees)	**Fees and charges**	**Nominal Return (Net of fees)**	**HICP**	**Real Return (Net of fees)**
2002	13.4%	16.1%	-2.7%	4.1%	-6.85%
2003	7.4%	5.8%	1.5%	6.9%	-5.37%
2004	13.6%	5.8%	7.8%	4.3%	3.46%
2005	8.2%	4.1%	4.1%	7.1%	-2.98%
2006	9.1%	3.5%	5.5%	5.7%	-0.20%
2007	16.2%	3.8%	12.4%	11.8%	0.59%
2008	-19.3%	2.5%	-21.8%	4.6%	-26.42%
2009	9.3%	3.0%	6.2%	1.6%	4.61%
2010	6.2%	2.5%	3.7%	4.4%	-0.65%
2011	0.6%	2.1%	-1.6%	1.9%	-3.47%
2012	8.6%	2.1%	6.5%	2.8%	3.74%
2013	5.9%	1.9%	3.9%	-0.9%	4.80%
2014	7.0%	1.8%	5.2%	-2.0%	7.23%
2015	2.5%	1.7%	0.8%	-0.9%	1.68%
2016	5.2%	1.5%	3.7%	-0.4%	4.10%
2017	7.0%	1.4%	5.6%	1.9%	3.72%
2018	-3.3%	1.2%	-4.5%	2.1%	-6.65%
2019	7.0%	1.3%	5.7%	3.2%	2.56%
Annualized since inception	**4.2%**	**1.8%**	**2.4%**	**1.6%**	**0.85%**

Sourse: FSC, HICP, BASPSC

(14) Data in table BG9 on page 131 is not correct.

Correct Figures are as follows:

Table BG9. Pension Funds and Pension Savers' Return (UPF)					
	2019	2017-2019	2013-2019	2010-2019	2001-2019
Pension Funds' Nominal Return (Gross of fees)	7.0%	3.5%	4.2%	4.4%	4.2%
Pension Savers' Nominal Return (Net of fees)	5.7%	2.2%	2.7%	2.7%	2.4%
Pension Savers' Real Return (Net of fees)	2.6%	-0.3%	1.8%	1.6%	0.9%

Source: FSC, NSI, BASPSC

(15) Graph BG11 presented on page 132 is not correct. The simple proof for the mistaken figures is that the inflation rate in a certain country for a certain period is the same regardless what type of investment return is calculated, either nominal or real. Obviously, this is not the case where inflation adjustments for the same time-periods are actually different for VPF and GPF in the report which makes the whole chart and conclusions wrong and unreliable!

(16) Graph BG13 plotted on page 133 is misleading. The Author compares **incomparable figures.** "Annual Insurable Income – real growth rate" is calculated as geometric mean, but "Pension Savers' Real Return (annual average)" is derived as Money-Weighted Returns

(17) The statement on page 134 that the "**report is the only** source, documenting the real pension savings returns across pension vehicles, available in Bulgaria, for the 2002-2019 period" is at least ambiguous. The Ordinance 61 of the FSC provides clear and methodologically proven concept of calculation and presentation of the real return to every member of the PF. That is sufficient proof that all pension funds are actually presenting upon

request **the real and reliably calculated returns** to its members (>3.5 million) on an individual basis in compliance with the instructions by the local regulator.

To sum up, we believe that in the analyzed material, the author skillfully works with statistics, creating manipulatively his thesis based on some facts, half-truths, wrong calculations and open speculative statements. There is no denying to the purposefulness, predefined talking points and the clearly biased approach, that we consider to be completely wrong.
The important and unacceptable deviations, errors and suggestions outlined above, definitely and unambiguously, indicate that the material can be defined as extreme and unreliable. It does not meet any standards and cannot be acknowledged as serious scientific studios, regardless of the significant numerical data, models and analysis used by the author, alas erroneously.
We are in agreement with the author that the supplementary pension system in Bulgaria needs to be further developed and more improvements have to be introduced rather sooner than later, such as:

- the introduction of multi-funds. Topic discussed for more than 10 years!;
- the timely regulation and quick approval of the already prepared pension pay-out phase legislation applicable for the UPF;
- enabling insured persons in UPF to choose a pension only from the SSS (State Security Institute) or a pension from the SSS and UPF at the last possible moment prior to retirement, similar to the rights of the insured persons in the PPF;
- a fair reduction of the pension by the SSS for the insured persons with supplementary pension form the UPF, taking into account the REAL contribution to the SSS system throughout the working experience of each insured person.

Management Board of BASPSC

NB! Please note all data and calculations provided in the tables are included in a detailed excel file, generated by the Pension Companies and can be provided upon request for reconciliation.