

Overview

BBVA Research¹

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In this work I analyze the relevance of considering a range of elements related to the investment process to evaluate the long-term returns of Pension Funds and the possible impact of these on the replacement rates of participants in a Pension System. The analysis focuses on Mexico for three reasons: 1. Its Pension System was not greatly affected in relative terms by the 2008 financial crisis; 2. The long-term returns of the Pension Funds (Siefore) in the System are considered a key variable in determining the pensions of participants; and 3. It was one of the first OECD countries to introduce a life-cycle scheme into its pension model.

The main result of this research is that the Mexican model of Siefores with diversified portfolios can offer reasonable returns over the longer-term, although it is not a control variable for the Pensions System. Once this limitation has been recognized, the only certain way that a pension or its replacement rate can be improved is to move towards higher contribution densities and to maintain appropriate contribution rates. If this is done, it is still possible to achieve additional improvements in pensions due to greater than expected returns. One route for achieving this is to increase the share of equity instruments in pension portfolios, which from a more wide-ranging perspective may also strengthen the Pension System as this alternative may also help to offset in part situations of low contribution densities by participants.

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