



# GCC Pension Fund Industry

STRICTLY CONFIDENTIAL



Amwal Tower, 22<sup>nd</sup> Floor, West Bay, PO Box 494, Doha, Qatar  
+974 4452 7777 • [am@amwalqa.com](mailto:am@amwalqa.com) • [www.amwalqa.com](http://www.amwalqa.com)

## Estimated pension fund assets (Mid-2015)

Countries	Pension Fund Asset (USD bn)	% of GDP	USD per national	% invested in local equities	% share of equity market
Bahrain	11	32%	18,000	19%	13%
Kuwait	65	38%	52,000	6%	4%
Oman	12	15%	6,000	22%	10%
Qatar	14	7%	51,000	70%	6%
Saudi Arabia	270	36%	13,000	24%	12%
UAE	25	6%	24,000	3%	1%
<b>GCC Total</b>	<b>397</b>	<b>24%</b>	<b>15,000</b>	<b>21%</b>	<b>8%</b>
UK (employer)	3,309	116%	55,000	5%	5%

Source: Ernst & Young's (EY) GCC Wealth and Asset Management 2015 report

## Reforms required to build a sustainable GCC Pension Fund Industry

### Major initiatives required to build a sustainable pension fund industry in the GCC

To address the concerns over the sustainability of the growing pension industry, GCC countries need to address issues such as the retirement age, contribution required and benefit levels.

- ❑ **Expansion of end-of-service benefit (EOSB) schemes or introduction of added pension security for expatriates and making funding of EoSB liabilities mandatory:** End of service liabilities are either under-funded or unfunded in majority of cases leaving expatriates vulnerable in the event of the bankruptcy of their employers.
- ❑ **Providing options for Shari'a-compliant retirement products:** Given an option, majority of GCC investors would choose Shari'a compliant product. Thus tailoring retirement products accordingly will provide major thrust to the industry.
- ❑ **Seek higher yields and lower volatility from investments:** Pension fund investment which are mostly concentrated locally should seek geographical diversification and better professionally managed funds. This would help in smoothening volatility and provide better returns.
- ❑ **Reforming the pension model:** Inadequate contribution rates and high benefit levels render pension structure unsustainable. Further payout to retirees at a staggering 80% of total government income from payroll taxes is going to place huge pressure on reserves and government funds given the GCC demographic shift. Introducing major reforms in the contribution rates and benefit levels in the Defined Benefit plan so that it covers primary living cost and supplementing it with an option for additional Defined Contribution plan to cover other costs would help in building a sustainable and mature pension market in the region.
- ❑ **Discarding monotony and opting for innovation and diversification:** Most GCC pension funds remain concentrated locally despite the market demanding greater sophistication, diversification and innovation in product development. The funds should not only diversify geographically but also across asset classes by investing in alternative assets (real estate, private equity), fixed income funds (diversified sukuk, trade finance, asset-backed leasing, securitisation) and other asset classes.
- ❑ **Eliminating restrictions constraining growth of pension assets:** Investment restrictions tend to constrain the growth of pension assets by devoiding it of the opportunity to invest in better growth markets and to diversify across asset classes. This could increase risk by way of concentrated exposure to a particular geography.

## Growth of DC-based Pension plans in the GCC

### Defined Benefit structure leaves the sponsoring employer with an open-ended funding liability

- ❑ Although gratuity liabilities are declared on the company's balance sheet, often the capital has actually been ploughed back into the business leaving gratuity obligations entirely unfunded.
- ❑ Most pensions professionals predict that persistent funding challenges will accelerate the closure of DB schemes and transition to defined contribution vehicles.
- ❑ Led by the UAE, the economies of the GCC have taken important steps in recent years towards creating more efficient retirement savings scheme for expatriates.
- ❑ Most companies are offering enhanced EOSBs in the form of separate defined contribution (DC) pensions or savings plan. Under such a structure, the value of employer contributions can be set against gratuity obligations, whilst at the same time employees have a cost effective and safe means of making additional voluntary contributions (AVCs).
- ❑ Most importantly, a trust-based scheme provides a means to legally separate any funds set aside to cover gratuity obligations from the actual assets of the business. This means that those funds are ring-fenced for their intended purpose, regardless of what the future holds for the business.
- ❑ According to survey conducted by Towers Watson, the proportion of companies offering a DC plan to all employees has increased from 34% to 48% between 2010 and 2014.

## Role of Pension in National development

### Private sector is expected to drive development in Pension industry

- ❑ Building a sustainable pension industry has the potential to play a key role in national development in the GCC.
- ❑ Introducing a state pension scheme for skilled foreign workers that meet specific criteria, in combination with easing retirement visa restrictions, may result in a higher number of expatriates choosing to remain longer and investing their savings within the local market rather than abroad.
- ❑ Establishment and expansion of private pension funds could help attract talent as well as boost capital market by channelling the funds thus aiding government's policy objective of developing equity market and deepening the debt market.
- ❑ Owing to low oil prices, GCC governments are under pressure to find new sources of funding for required investment in infrastructure projects. Pension Funds can help in developing the infrastructure bond market thus aiding project financing resulting in funding the cash strapped GCC infrastructure.
- ❑ A developed and mature Pension industry would result in multiplier effect in the economy resulting from investment in infrastructure projects, etc. Multiplier effect, in which increase in spending produces increase in national income and consumption, is a major source of economic growth.

## Regulatory and Operational Challenges

### Regulatory Challenges

- ❑ To ensure compliance with pension plans laws and regulations, appropriate oversight and reporting, and safeguarding of the plan investments.
- ❑ Dealing with solvency and unfunded liability issues, particularly with those pension plans that are funded by collective agreements.
- ❑ Selecting the governing body and shielding funds from political Interference. Establishing internal governance structures and processes aimed at minimizing corruption, mismanagement, and fraud.
- ❑ Enhancing pension system coverage in both mandatory and voluntary schemes.

### Operational Challenges

- ❑ Helping the greying population to maintain a sustainable consumption smoothing is a major challenge both for funded and unfunded pension schemes.
- ❑ Under some schemes, benefits currently being paid are higher than the contributions received. Inequality between the contribution rate paid and the benefits promised is expected to cause financial strains in the future.
- ❑ Creating a retirement savings structure for each business that balances the employer's need for controlled risk and affordability with the level of flexibility needed to help employees bear their own responsibility for retirement.
- ❑ Data and analytical tools are needed to better understand pension fund members and drive member engagement. This can be achieved through better segmentation, customization of propositions, services and communications strategies and development and implementation of retention strategies.
- ❑ Enhancing administrative efficiency to minimize running costs of the pension system.

## Extending Pension scheme to expatriates will help bolster Pension Industry

**GCC's policy of excluding expatriates from its pension programme is negative for future economic development**

GCC Countries	Year of Data	Local (% of Total Workforce)	Expatriates (% of Total Workforce)
Saudi Arabia	2014	22%	78%
UAE	2015	15%	85%
Qatar	2012	6%	94%
Kuwait	2015	17%	83%
Bahrain	2015	23%	77%

- ❑ Expatriates account for more than three fourth of the total GCC workforce. Introduction of mandatory pension system for the expatriates would result in directing the savings, which would otherwise be remitted abroad, into the regional capital markets, real estate and infrastructure sector and other asset classes thus aiding the economic development of the region.
- ❑ This would also enhance the region's capacity in attracting and retaining talent who in turn would help in driving the economic growth.
- ❑ In the current environment of low oil prices where most funding sources are drying up, a developed and growing pension industry could act as a major funding source for various projects required for growth in the region.

Source: Saudi Department of Statistics and Information, Gulf Digital News, BQ magazine, Gulf Times



## Amwal LLC

Amwal Tower, 22<sup>nd</sup> Floor, West Bay

PO Box 494, Doha, Qatar

Main: +974 4452 7777

E-mail: [am@amwalqa.com](mailto:am@amwalqa.com)

<b>Fahmi Alghussein</b>	CEO	+974 4452 7500	<a href="mailto:falghussein@amwalqa.com">falghussein@amwalqa.com</a>
<b>Hani Abdo</b>	COO	+974 4452 7777	<a href="mailto:habdo@amwalqa.com">habdo@amwalqa.com</a>
<b>Talal Samhouri, CFA</b>	Head of Asset Management	+974 4452 7555	<a href="mailto:tsamhouri@amwalqa.com">tsamhouri@amwalqa.com</a>
<b>Kamlesh Kasala, CFA</b>	Risk & Compliance Director	+974 4452 7506	<a href="mailto:kkasala@amwalqa.com">kkasala@amwalqa.com</a>
<b>Mohamed Abdulla Al Mualla</b>	Vice President	+974 4452 7523	<a href="mailto:malmualla@amwalqa.com">malmualla@amwalqa.com</a>