Abstract

Lifecycle Portfolio Modelling in Funded Defined Contribution Pension Systems

RESEARCH PAPER

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The implementation of funded defined contribution pension systems prompted a broad discussion on how to protect pension fund members from the various risks associated with capital markets. Investment risk management is traditionally carried out by investment rules (mainly investment restrictions). However, in single portfolio systems that allow pension savings in just one fund or a single portfolio for all members without making a distinction as to age, these rules are not adequate to prevent the timing risk, namely a sudden fall in the value of accumulated savings immediately before retirement. Consequently, new methods of lifecycle portfolio modelling have been developed. These new investment strategies are based on the age of retirement. Therefore, in this paper the authors analyze the different modalities of lifecycle portfolio modelling from the theoretical and comparative perspective. Two main model strategies have been highlighted: the model of funds of different risk levels (so-called lifestyle funds) and the model of target date funds (so-called lifecycle funds). Knowledge about and understanding of these strategies is important for the successful implementation of the three pillar pension system in Croatia, where two pillars are funded defined contribution systems.

Keywords: lifecycle funds, lifestyle funds, target date funds, pension, pension insurance, defined contribution schemes, funded defined contribution, investment risk
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