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FULLY FUNDED PENSION SYSTEM IN SIX NON EU BALKAN COUNTRIES

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Abstract

The goal of this paper is to review the situation with fully funded pensions system in six countries on the Balkan Peninsula: Albania, Bosnia and Herzegovina, Kosovo, Montenegro, Serbia and the Republic of North Macedonia. The observed countries, except Kosovo and the Republic of North Macedonia, did not accept a mandatory and voluntary fully funded pension insurance system for various reasons. While there are many advantages of private fully funded pension insurance - primarily diversification of risk, better protection against political pressures, possibility to develop financial market and so on, there are also surveys that show relatively weak positive effects of such system. Pension funds in the observed countries face important challenges regarding the asset allocation. Government securities and bank deposits represent still a large part of the portfolios of the pension funds. The process of efficient private financial risk sharing can be significantly accelerated by preparation for EU membership.

Keywords: funded pension system, pension reform, balkan countries

1. INTRODUCTION

A multi-pillar private pension schemes can become an important source of funds for investments, while the alternative pillars can actively contribute to

economic growth and better protect individual contributions for future pensions (OECD, 2018) primarily through the higher rate of return than under than public intergenerational solidarity (Palacios and Whitehouse, 1998). Diverse approaches towards funded pension insurance system chosen by different countries can be explained by the variances in their institutional capacities, and by the diverse ambitions driving the reforms. Furthermore, shifting from a present mature PAYG model to a fully funded system is an essentially different scenario, involving diverse demanding and complex issues. The goal of this paper is to provide insight to the situation with fully funded pensions system in six countries on the Balkan Peninsula: Albania, Bosnia and Herzegovina, Kosovo, Montenegro, Serbia and the Republic of North Macedonia. Unlike Bulgaria, Croatia and Hungary that previously accepted a mandatory and voluntary fully funded private pension insurance system, the observed Balkan countries, except Kosovo and the Republic of North Macedonia, did not do it for various reasons. Although similar at first glance as transitional countries with relatively weak institutional support, the differences in mentioned countries in relations towards their pension system and its reforms are very pronounced. Importance of our contribution reflects in the fact that, according to our knowledge, this is the first attempt to describe and compare fully funded pension systems in the observed countries in one paper.

Having in mind the result of economies of scale and the possible gains from the larger financial stock and flows that the sector has to administer, Holzmann (1998, p. 25) believes that the fact that the contributions for fully funded pension insurance system managed by the private financial sector would make financial market more liquid, deeper, and more competitive. The higher efficiency would boost investment and growth. However, the overall effect on national saving mostly depends on the behavioural responses of employees and government as well as on characteristics and the operational particulars of the pension privatization itself. Orszag and Stiglitz (1999) show that, depending on these partial effects, the overall effect on national saving and related economic growth could be positive, negative, or neutral. Altiparmakov and Nedeljkovic (2016) find no evidence that privatization of the pension system in the South America and Eastern Europe was associated with higher economic growth. They underline that often in the reformer countries in the South America and Eastern Europe second pillar accumulated funds invest most of their assets in government bonds that were issued primarily with an intention to finance transition costs. Their results of savings regressions are very similar to Schwarz and Arias's (2014) survey that debt-financed transition is unlikely to increase savings.

With different idiosyncratic characteristic, pension reforms in the Southeast and Central Europe former socialist countries have mostly followed a multipillar approach in the reforms of pension insurance. This includes a strong earnings-related PAYG component (public pension systems); mostly compulsory capitalized models of various sizes; and tax-induced voluntary pension schemes. In the period between 1998 and 2011, 11 countries in Europe introduced

multipillar pension reforms. The Czech Republic accepted a mandatory funded model in 2013. Performance of pension systems varied, but most of the countries succeeded to offer positive real returns. The financial crisis from 2008 caused significant temporary losses on the majority of the pension funds, but most funds successfully recovered part of the loss the following year (Schwartz and Arias, 2014).

There were some serious analysis and proposals for introducing of mandatory fully funded system in six observed countries on the Balkan Peninsula (for example for Montenegro, Government of Monte Negro, 2013; for Serbia, Mijatović and Hiber, 2008), but a majority of these countries began only with development of voluntary funded private pension insurance. Such retirement savings are becoming a vital aspect of pension systems in many countries, including a majority of six observed countries (Altiparmakov, 2013). While voluntary retirement saving model can produce significant economic benefits, they are mostly limited to citizens with above-average earnings and living standards that can afford to make additional retirement savings. Tax incentives and/or exemptions for the third pillar of pension insurance certainly have an impact, but much less than expected when such insurance was introduced. In the fiscal literature, there is a long-term and ardent debate about the real effectiveness of tax incentives for all kind of human behaviour and business activities, including participation in voluntary pension insurance (Poterba and Samwick, 1999).

Next to the diverse legal, organizational and institutional solutions - primarily regarding the existence of mandatory and voluntary fully funded pension system - the observed countries also differ in the availability of published data, but generally there is a serious lack of long-term statistics particularly about the returns from invested sources. The hypothesis is that the introduction and/or the development of the fully funded pension insurance systems in the observed countries would reduce the financial burden of the PAYGO system and in that way improve its long-term financial sustainability. Furthermore, the fully funded pension insurance systems should have important auxiliary effects on the increase in the amount of the average pension, improve the weak relation between paid contributions and achieved pension rights, motivate people to stay longer in employment, and finally, contribute to the development of the financial market. After this introduction, follows the review of six countries. The observed countries are presented in the alphabetical order. Section 3 contains discussion, while Section 4 deals with conclusions. For easier mutual comparison, we added the Annex 1.

2. REVIEW OF SIX COUNTRIES

Albania

Albania is a relatively young country but it is rapidly aging due to emigration of key working age population. The current pension system is dominated by a hardly sustainable state pension system (first pillar) (The World Bank, 2014). There is no mandatory (second pillar private pension saving) in

Albania, but there is a small voluntary pension system (third pillar). Xhumari (2010) believes that the reason why Albania did not introduce the mandatory fully funded pension insurance is related to the influence of the political factor, as it was considered too early to introduce the privately managed pension schemes after the negative experience of the financial pyramid schemes collapsed in 1997. The Socialist government came to power in 1998 with the promise to give the money back to people who lost it at the pyramidal schemes and they could not fulfil their promise. Furthermore, as the first PAYG pillar was not sustainable; the professionals of the Social Insurance Institute were supporting the idea of strengthening the first pillar rather than investing in the second pillar.

After political change in 2005, on 1 January 2006, first two institutions offering private pension model started to operate and two months later a third one started, (Poteraj, 2012). According to The Financial Supervision Authority (2018), one participates in the total capital of all pension funds' investment portfolio 87.7% while other two with 6,5% and 5,9%. The voluntary pension market has shown significant development with the inclusion of appropriate fiscal incentives in the 2015 fiscal package. The employer and employee contributions to the voluntary pension insurance funds are treated as non-taxable income, up to the legal limits, and are reflected in the payroll. The voluntary private pension funds at the end of 2017 had total net assets of EUR 12.99 million. During 2017, the investments of the pension fund market consist of treasury bonds of the Republic of Albania with a maturity of 3, 5, 7 and 10 years. In the total market, investments in government bonds with a maturity of 7 years and 10 years are those that occupy the largest share and account for respectively 35% and 47% of the total assets of this market. Albania has created the Albanian Stock Exchange only recently, which may enable a greater diversification of pension fund assets that are presently almost fully invested in government bonds (OECD, 2018).

International evidence typically shows that equity markets offer a much better long term-return compared to other investments. However, the question of domestic versus international investments can be politically difficult but without doubt forcing a fully funded pension funds to invest all resources in Albania would be counter-productive. Without a proactive programme of capital market expansion, the development of private savings is not likely to benefit the domestic economy and its growth as it could. Strengthening of the domestic capital market helps provide better options to solve the international versus domestic problems. Even though in a small market 100% domestic investment will always be risky.

In Albania, there has been a significant progress on a range of the pre-conditions for a private pension insurance system. The introduction of the new voluntary fully funded system shows that both the legislation and the institutions can be created. However, it is currently very small and one should keep in mind high levels of distrust in financial services in Albania. The Government (Republic of Albania, 2013) expressed its intention to encourage and develop the second pillar of the social insurance system, however without further actions on the reform (Hysa, 2014).

Bosnia and Herzegovina

The Dayton Peace Accords from 1995 retained Bosnia and Herzegovina's international boundaries and created a multi-ethnic and democratic government charged with conducting foreign, diplomatic, and fiscal policy. Also recognised was a second tier of government composed of two entities roughly equal in size. The Federation and Republic Srpska (RS) governments are responsible for performing most government functions, including control of the pension system. The two entities have separate pension funds, and the pension systems are regulated by separate legislations.

The Federation

The Law on Voluntary Pension Funds - VPFL has been enacted in July 2017, with all supplementary acts prepared and published by end-2017. Surprisingly, no licenses for pension fund management have been either issued or applied for during 2018. The World Bank team that visited B&H discussed with the counterparts, the reasons for such an outcome (The World Bank, 2019). One of causes is that the VPFL is requiring that a majority of the voluntary pension fund administration company is held by a commercial bank or insurance company. Such a provision has disqualified the existing investment fund managements companies. Furthermore, a rule that a commercial bank providing depository services to a private pension fund must not participate or be related to the pension fund administration services additionally reduces the list of potential actors. Second, stimulating tax treatment of voluntary contributions has not been enacted. Third, the public awareness about the voluntary pension savings is exceptionally low.

Republic Srpska

Pension Reserve Fund - PREF was established in 2011 as investment fund with the purpose to manage assets of the first pillar and assure its sustainability. The core investment principles set by the legal framework are the security principle (financial instruments with high credit ratings, i.e. low risk on the domestic capital market), the principle of diversification, liquidity principle and the principle of profitability. In the period from 2011 to 2017 were achieved total assets in a value € 115,504,712.16. Available assets have following structure according to risk range: 80.51% with low risk, 2.27% with moderate risk and 17.22% with high risk. More than a third of the assets of the Fund is in bonds issued by the RS or its municipalities (The Srpska Times, 2019). Despite the law on voluntary pension funds was passed in 2009, only eight years later, in 2017, the first voluntary pension fund management company in the RS and Bosnia and Herzegovina was established. Employers are exempt from payment of the company income tax and contributions for pension insurance on the gross salaries

of their employees, if they pay annually up to a maximum of € 613 in voluntary pension fund. Government promotes participation also through monthly contributions for all public employees that receive salaries from RS budget since January of 2020. However, the years ahead are crucial for the success of this project.

Kosovo[1]

Kosovo faced many of the same problems as other transitional countries when establishing their new pension system. The country is small and there has been limited local capital market. The labour market is characterised by a mixture of formal and informal sectors and there has been limited capacity among government, industry and the population to resolve the complex problems of pension insurance. The case of Kosovo has been unique given that it did not inherit any pension system or any funds for retirement age. In contrary, it had to establish the pension system from the beginning and at the same time, introduce policy options, which would be in line with present social and economic conditions (Havolli and Morina, 2016). Therefore, the landscape of fully funded pension insurance in Kosovo is a little different as the country has also the second mandatory pillar with defined contributions. The idea to introduce three-pillar pension system has goal to provide a reliable source for retirement income; to reduce the financial demands on governments; to increase local savings; to provide a stable domestic source of financial resources needed for economic development; and to encourage the development of local capital markets (Sejdiu, 2018). The country was even blamed to building a pro-market, liberal model of pension insurance (Xhumari, 2010).

Therefore, the first pillar is a Base Pension, where the government of Kosovo from its budget pays a pension (of 40 € monthly) to each citizen of Kosovo over the age of 65 years. The second pillar is a system of individual savings that is compulsory contribution to Kosovo Pension Savings Trust (KPST), which became operational in August of 2002. The third pillar is Supplementary pension system stimulated by tax relief. While in the first pillar an old age basic pension and disability pension are funded from general tax revenues, in the second pillar employers and employees each contribute 5% of salary to the KPST. It is a long-term investor with the primary objective to ensure that assets are invested in a prudent manner consistent with the requirements of the Law. The value of assets increased until the end of 2017 to €1,656m (The Kosovo Pension Saving Trust, 2018). Both the second and third pension insurance pillars are regulated by the Central Bank.

On the debate related to the investment strategy of KPST there were many alternatives discussed, among the investing the funds in the domestic

[1] This designation is without prejudice to positions on status, and is in line with UNSCR 1244 and the ICJ Opinion on Kosovo declaration of independence.

economy which was more immune to the crisis given its limited exposure. However, investing the KPST into the domestic economy would be practically impossible due to the lack of instruments in the financial markets of Kosovo (Havolli and Morina, 2016). Although the scope for voluntary pensions in a small country like Kosovo with high informal sector is very limited, there is still one private pension fund in operation offering voluntary pensions since 2006. Contributions if paid by company are deductible for the company income tax, while if paid by individual are deducted from gross salary and deductible from personal income tax. The model of the pension system adopted in Kosovo had a number of good and unique features, which may not be all suitable for other countries. The World Bank (2014) stresses that the Kosovo experience maybe helpful in understanding the required practical steps needed in the establishment of a new pension system - from design to the development of techniques of collection and IT systems.

Montenegro

Although announced by the government of Montenegro (Montenegro Government, 2013), the second pillar has never been introduced, while the third pillar was established by the Decree on Proclamation of the Law on Voluntary Pension Funds. The Law governs the conditions for establishing pension fund managing company and organizing voluntary pension funds based on individual capitalized savings as well as their operating. The Securities Commission in compliance with provisions of this Law and the Law governing securities performs supervision over foundation and operations of Pension fund Management Company and Pension Funds.

Montenegro is a rare example of a country providing no financial incentives for investing in voluntary pension funds. The Council for the Improvement of the Business Environment, Regulatory and Structural Reform in 2013 has formed a working group for the analysis of the effects of introducing tax exemptions and/or deductions for membership in voluntary pension insurance funds. The working group has presented its report in 2014 and underlined the importance of development of voluntary pension funds. However, having in mind the current situation of public finance, the working group did not support the introduction of tax exemptions and/or deductions for membership in voluntary pension insurance funds (Komisija za hartije od vrijednosti, 2018). It is hard to assess the accuracy of Savković and Dožić (2018) statements about the non-existence of tax incentives as the main cause of failure of voluntary pension schemes in Montenegro, but at least some small steps, in this direction will be fruitful and welcomed. If the government is against tax exemptions and deductions due to the intention to protect the simplicity of the tax system, co-financing payments to the voluntary pension insurance may have the same effects.

Two voluntary pension funds were established and at the end of 2017; one had 2,166 members and total assets in value €493,890.80, while the other had 222 members and total assets in value € 60,686.31. The assets of 2,251 members of the voluntary pension fund "Penzija plus" were temporarily frozen and the payments and disbursements from the fund were blocked, as their custody bank, Invest Bank Montenegro, has been bankrupt since the beginning of 2019. The Fund's assets by law do not enter the bankruptcy mass of custody bank, but trust in the system can be negatively influenced.

Serbia

Serbia accepted the Law on voluntary pension funds and pension schemes (OG 85/05 and 31/11) and necessary by-laws. The Law stipulates organization and management of voluntary pension funds; founding, business activity and business operation of a Pension Company managing a voluntary pension fund and activities and obligations of a Custody Bank. Furthermore, the Law defines authorities of the National Bank of Serbia (NBS) in supervision of operation of pension companies, which manage pension funds and pension schemes; and other relevant issues. Assets may be invested in debt securities issued by the NBS and the Republic of Serbia (without limitations), in corporate debt securities (up to 50%), in shares (40%), money deposits (35%), investment units of open-end investment funds (5%), real estate (5%) etc. Total investment of fund assets abroad under all grounds may not exceed 10% of fund assets. Employees and employers can save up since their contributions up to € 50 per month are exempt from the personal income tax and contributions for mandatory social insurance.

At end of 2018, the market of voluntary pension funds included four companies managing seven VPFs, one custody bank and five agent banks (The National Bank of Serbia, 2018). Net assets expanded reached € 341 m. According to the size of VPF net assets relative to total net assets of the sector, two funds were classified as “large” and two as “medium”. Together, they held 95% of the market share, with the largest fund accounting for around 40%. Government bonds accounted for the major part of VPF assets - 83.1%. At the end of 2018, for the first time since the start of VPF operation, 0.2% of total assets were invested in shares of foreign legal entities abroad. At end of 2018, 192,295 users were in the accumulation phase. Total membership contracts in VPFs stood at 261,726. Individual payments accounted for 34%, employer contributions for 30% and pension schemes for 36%.

The North Macedonia

From the all observed countries, next to Kosovo, only the North Macedonia has fully developed systems embracing all three pillars: the defined benefit public PAYG system, privately managed second pillar of individual

retirement accounts and third-pillar voluntary pension funds. Public pensions face significant sustainability and fairness issues with a deficit of 4.4 percent of GDP in 2016. The second pillar is governed by the Law on Mandatory Fully Funded Pension Insurance from 2002 and it started in 2006. The third pillar is governed by the Law on Voluntary Fully Funded Pension Insurance from 2008 and it started in 2009. Private pension accounts, contributions and assets under management have grown rapidly since 2006, with the vast majority arising from the mandatory second pillar rather than the voluntary third pillar.

Workers with a 'first employment' after 2003 were mandated to join the new multi-pillar system, with their employer contributing 12 percent of wages to the public and 6 percent to mandatory private pensions on their behalf. Before 2018, workers with a first employment before 2003 could opt to join the new system and contribute as above or remain in the first pillar only. The post-2003 generation (and switchers) were placed at a significant disadvantage in relation to future public pension entitlements. This stipulation has been changed with the new regulation from 2018, so instead of the first employment, the members of mandatory pension insurance are those that in the moment of starting with contribution for the second pillar (2008) were younger than 40 years of age and other that opted in, have a possibility to stay. Taxation follows the 'Exempt-Exempt-Taxed' (EET) approach: contributions and investment gains are not taxed (subject to a limit on maximum permissible contributions per year) but pension pay-outs are taxed.

At the end of 2017, total private pension assets were €936 million, with 98 percent of assets in second pillar funds. Total assets have been growing strongly in recent years and are now approaching 10 percent of GDP. The two private pension providers have been able to gain economies of scale in a small market. Both companies have been active since 2006 for mandatory pensions and 2009 for voluntary pensions, with no changes to the institutional landscape in the first 10 years. The market is evenly split between the two companies, with each approaching 250,000 members and assets under management in value €450 million. (Agency for Supervision of Fully Funded Pension Insurance, 2019). The split of market between only two companies helps each achieve reasonable economies of scale even in a relatively small market. The third fund is in the registry from 2018 but it did not yet start to collect members. There is an allocation rule for workers who do not choose a provider, so the mechanism leads to a pretty even split between the two companies as they charge similar fees and have similar investment returns. This approach should be continued, building on the adjustments that have been made to allow new entrants to gain market share. A critical step should be to avoid marketing and sales wars that create high levels of switching of members, having negative impacts on costs and investment allocations as higher liquidity is required to meet demands for account transfers.

International diversification has been growing over time, with 28 percent of assets now invested outside of the country. The North Macedonia has a relatively high allocation to foreign assets, a mid-range allocation to government

bonds but a relatively high allocation to fixed deposits and low to domestic corporate bonds, reflecting the relatively under-developed nature of the domestic capital market in which corporate bond issuances are minimal. The Agency for Supervision of Fully-Funded Pension Funds (MAPAS) supervises Pension Funds and Pension Companies and submits an Annual Report on the Operation of the Agency to Parliament.

3. DISCUSSION

Fully funded system of pension insurance provides a high degree of transparency, which is one of the most crucial and positive features in the pension system (Mustafai, 2017). Within the observed group of countries, only Kosovo and the North Macedonia have started with a comprehensive multi-pillar reform. Others have been planning it, but most of them, for the time being, are combining the public PAYG systems with the third private voluntary pillar. Therefore, assets under management of fully funded pension funds in GDP differ significantly in the observed countries (Table 1).

Table 1

Assets under management of pension funds, % of GDP, 2017

Albania	BH-federation	BH – Rep. Srpska	Kosovo	N. Macedonia	Montenegro	Serbia
0.1	0	0.01	27.52[1]	9.2	0.01	0.70

Sources: various national documents mentioned in the national overviews, particularly OECD, 2018.

1) Data for Kosovo GDP are taken from https://tradingeconomics.com/kosovo/gdp-constant-prices

Transition costs of pension system reform gross or maximum transition costs are equal to contributions redirected to the second pillar. If the pension system reform enables positive externalities (higher economic growth due to development of capital markets, improved tax compliance, etc.), net transition costs may be smaller than gross transition costs. The remaining deficit (transition costs) may be covered in different ways, which determines the direction of intergenerational redistribution (Šonje, 2011). Pension reforms, around the world, and particularly in six observed countries, are aimed at increasing retirement savings in countries where these are still low and provide incentives for sufficient diversification in equities and across countries, as well as measures to reduce obstacles to cross-border pension funds' consolidation and enhance the efficiency of private financial risk sharing (European Central Bank, 2018). Impact of a funded pension system on capital markets should have positive effect in national savings and investment as well as on improvement of financial competition and financial market expansion. This process should be accompanied by strengthening of financial regulation, which means a better protection of the individual investor what is a basic premise of fully funded schemes.

Most of observed countries have relatively small coverage and mostly underdeveloped voluntary pension savings. In the voluntary pension fund, membership is by choice of the individual person or through participation in a pension scheme funded by the employer or an association. The interest for the third pillar is not necessarily linked to the fact that the country has the second pillar of mandatory pension insurance. Voluntary pension savings are simply less attractive than others savings possibilities, regardless of what are the potential benefits. People will put money on bank deposits accounts and/or invest in real estate rather than in voluntary retirement savings. Possible reasons could be easier liquidity, distrust towards the finance sector (Albanian chains of happiness, the foreign exchange deposit freeze and financial scam pyramid systems in B&H, Montenegro and Serbia), lack of knowledge and information. According to the older survey of the popularity of the third pillar in comparison with other forms of pension insurance, the third pillar has the lowest level of acceptance (Börsch-Supan and Miegel, 2001).

All observed Balkan countries except Montenegro exercise tax reliefs or subsidies for voluntary pension contributions. However, there is no evidence that the tax treatment of voluntary pensions has a significant impact on voluntary pension savings. In addition, there are concerns about the redistributive features of tax reliefs and subsidies for voluntary pension contributions, as they may have been directed towards the higher income wage earners. Further analyses would be needed in each country to determine the optimal tax treatment of voluntary pension contributions.

Awareness and financial literacy have a role, but less than expected (van Rooij, Lusardi and Alessie, 2011). In many post-transitional countries, public campaigns for the third pillar have showed great expectations, but the real effects have been usually limited. In addition to distrust, there is a great myopia and widespread inertia. Probably better solution would be auto-enrolment of all employees in the voluntary insurance with the possibility to opt-out.

The technical aspects and legal stipulations of the third pillar of pension insurance - regarding the structure of investments, fees, limits, risk sharing and so on, as well as the profitability of included funds - did not prove to be decisive factors either to demand for enrolment or the interest of companies from financial sector to provide such services (Cook and Johnson, 2000). Although not crucial, such factors should not be neglected, but should be considered during the legal and organisational preparation for establishing and broadening of the second and the third pillar of pension insurance (Giannetti and Laeven, 2009).

Observed six countries are characterized mostly by the relatively undeveloped (illiquid) capital market. Furthermore, mostly they have young regulatory institutions and a relatively inefficient legal system in general. Rare studies - for example, Hryckiewicz (2009) - point to the significant impact of the reform of the pension system and the capital market on economic growth,

primarily through the development of the financial market and the improvement of capital market regulations.

Pension funds in the region face important challenges in the area of asset allocation. Government securities and bank deposits are still a sizable part of the portfolios of the pension funds. On average, they represent approximately two-thirds of the pension portfolios in a selected group of countries in the region that conducted pension reform. Most countries need to move toward better diversification of assets in order to effectively diversify the future pension risk of individuals. Traditionally pension funds in EU have invested a lot in fixed income, but over the last decades, they have started to shift towards equities and alternatives. At present, there is significant heterogeneity in the asset allocation among EU member states, with respect to direct or indirect holdings of equity in particular (Amariei, 2018). Diversification of pension portfolios into equities, corporate bonds, mortgage bonds, and international securities is essential to ensure that the repayment capacity of the state does not affect pensions of unfunded and funded systems. International diversification allows diversification of the sovereign risk, which allows contributors to hedge against country-specific idiosyncratic risks (Schwartz and Arias, 2014).

Needed progress in private financial risk sharing cannot be quickly achieved as many measures would take a long time to unfold their effects. However, the process can be significantly fastened by preparation for EU membership that should have a positive impact on the development of their financial markets and sustainability of their fully funded pension systems. The reason is that, according to Darvas and Schoenmaker (2017), European Union membership may foster financial integration and reduce information barriers in investment, which sometimes limit cross-country diversification. Their panel regression estimates for 25 advanced and emerging countries in 2001-2014 provide strong support for the hypothesis that the larger the assets managed by institutional investors - including pension funds, insurance companies and investment funds - the smaller inclination the home bias investment and thereby the greater the scope for risk sharing.

4. CONCLUSIONS

The pension funds are responsible for activities, innovations and liquidity on capital markets, and thus, with banks and insurers, are the most significant participants in financial markets. As a final message, one could reiterate the most important conclusions. There is a close relationship between the pension system and the capital market, which is evident in developed countries, and in countries where fully funded system has been introduced. Fully funded pension funds, with the significant assets under management, are crucial institutional investors in the capital markets of developed economies. However, the impact of fully funded pension system and funds on the development of the capital market and economic growth should be assessed in longer period.

In all observed countries, there is a need to develop the pension system by liberalizing the market and ensure improved regulation of the pension funds. Furthermore, it is important to liberalize and/or remove restrictions on investment options and develop adequate instruments, which can provide adequate possibilities for pension fund administrators to invest prudently in the local market. There is an obvious need to ensure an efficient flow of information provided by financial suppliers to consumers. In that way clients are empowered to make informed financial decisions that would meet their needs and benefit them in the long run. In observed countries, consumers are not fully aware of possibilities and limits of the fully funded pension system. Thus, the Government and its bodies can help in organising education professionals to provide free of charge, independent and reliable services on financial planning and providing advices to help citizens who do not possess enough knowledge to cope with the complex range of financial products. Furthermore, it will be very fruitful to organise and conduct programmes of financial literacy for citizens and a public campaign to raise awareness about this form of savings.

Citizens should not have unrealistic expectations of the public pension systems and the state in general. To the working age population, it must be clear that they themselves to a greater extent should take care of their old age and that later they cannot and must not blame someone else for not having saved enough while working. Therefore, according to all that has been said, it is necessary to systematically develop and promote fully funded pension insurance.

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Annex 1

Basic data on funded pension systems in six observed countries

	ALB	BH-FED	BH - RS	KOS	MAK	MONT	SERB
Coverage % of workers	1.87%	0	1.30%[2]	352,849 (mandatory, active) 41,823 accounting units (voluntary) Total 394,672 - most of the insurees are insured in both forms, so there is significant double accounting.	83.6	1.30	12.28
Assets under Management – AUM, in EUR Million	12.99	0	0.29[3]	1,656 (mandatory) 7 (voluntary)	936	0.55	341
Year of inception	2006	The Law on Voluntary Pension Funds (VPFL) in the Federation B&H has been enacted in July 2017	The Pension Reserve Fund established in 2011. First Voluntary Pension Funds established in 2017	Kosovo Pension Savings Trust has been established in 2001 and became operational as of August of 2002. Voluntary insurance was licensed in 2006.	The second pillar is defined by the Law from 2002 and it started in 2006. The third pillar is regulated by the Law from 2008 and it started in 2009.	The Law on Voluntary Pension Funds is from 2006. The first voluntary fund *Penzija Plus* obtained the permission for work in 2008.	Serbia in 2005 accepted the Law on voluntary pension funds and pension schemes (OG 85/05 and 31/11) and necessary by-laws.
Number of funds	3	0	1	1 mandatory 1 voluntary	Mandatory and voluntary insurance 2 active (1 is preparing)	2 voluntary funds	7 voluntary funds
Average fund account in EUR	620	0	82	2,800 (mandatory, if all accounts are used) 4,693 (mandatory, if only active accounts are used) 168 (voluntary)	Mandatory insurance 2,478 (Sava) 2,623 (KBP mil) Voluntary insurance 1,306 (Sava) 959 (KBP mil)	232.23	1.303
Rates of return – RoR, since inception	3.7	0	1.3	All forms 5.4 (OECD, 2019a) Mandatory 2.17 (KPST, 2018)	5.3% in nominal terms and 3.3% in real terms	For *Penzija plus* in 2016 +5%, in 2017 - 3.3%. *Market Penzija* in 2017, +4.9	8.1
Administrative fee, latest	The fees charged in 2013 were 3% of assets under management a year. There were	According to article 30, management fee consists of a) the fee for the payment of pension	According to the Law on voluntary pension funds and pension plans in RS, the fee consists of: a)	Mandatory insurance: Operating fees: 0.071% per year; and b) Investment fees: 0.381% per year.	At the start of the second pillar (2006), contribute-on fees were 8.5% and AUM fees 0.6%t per	Manageme nt fee is 3% of paid contributio ns and 2.5% of the total assets of the	The contribution fee is paid only once, as a front-load fee. The level of the fee in

	no additional entry fees or on-going fees. There was a fee of 0.5% to transfer to another provider. There was a system of penalty fees for members who want to withdraw their money from their pension.	contributions, not more than 3% of the value of the payments; b) fund management fees, not more than 2% per annum from the net asset value of the voluntary pension fund. Costs related to the purchase, sale and transfer of securities and the cost of services of depository banks are charged from the property of the voluntary pension fund.	remuneration for the payment of a pension contribution, up to a maximum rate of 5% of the payment value and b) voluntary pension fund management fees, up to a maximum rate of 2% annually from the net asset value of the voluntary pension fund[1].	Voluntary insurance: the annual management fee is 1.5% of the total Fund's assets. Entry fee is 3% of monthly contribution, while exit fee is 1%–2% a year of the total amount.	year. As of January 2020, the fee was 2% and the AUM fee 0.36%. For voluntary insurance as of 2017, the contribute-on charge was 2.9% for both providers. NLB charges a 1.2% per year AUM fee, whilst KBP charges 0.9%.	pension fund. Exit fee is 2% of the funds on the personal account of the fund member.	Q4 2018 was 1.94% on average.
Portfolio, % of G bonds	94,7% (OECD, 2018a)	0	More than a third of the assets of the Fund is in bonds issued by the Republika Srpska or its municipalities	Mandatory insurance 35% in Kosovo treasury bonds & other bond funds. Voluntary insurance 5% for stocks and 30% for bonds. No such limitation applies for Securities of Government of Kosovo.	Mandatory insurance: bonds of domestic issuers 49.72 (Sava) 59.06 (KBP mil)[8] Voluntary insurance: bonds of domestic issuers 38.75 (Sava) 50.44 (KBP mil)[8]	Legal possibility to invest all assets in G bonds	Government bonds accounted for the major part of VPF assets -– 83.1% in Q4 2018. .
Eligibility age	Article 16 stipulates that 1) A pension fund unit-holder, upon his choice, shall have the right to receiving immediate payout of the net value of assets in his or her account, or periodical payments in pension form, corresponding to that value: 2) When he or she reaches the retirement age prescribed by the law for the mandatory pension system;	Article 104, 58 years of life	The right to withdraw and dispose of accumulated assets is acquired with 58 years of age without considering the period of accumulation of funds, or with 53 years the age of and at least five years of accumulation in continuity or 60 monthly payments in accumulating funds. Withdrawal and disposal of accumulated assets by a voluntary member the	Article 1 stipulates Pension Age at 65 years.	For voluntary insurance 10 years earlier than legal retirement age.	50 years of life	Article 62 defines that a member of a voluntary pension fund, and/or pension scheme is entitled to withdraw and use pooled pension funds upon turning 58 years of age.

	c) 5 years before the unit-holder reaches the retirement age; d) upon the unit holder's permanent disability causing him or her to be unable to work, as certified in accordance with the applicable law.		pension fund must begin at the latest with 70 years of the age (Article 74).				
Lump sum allowed?	No, but there is a possibility of early withdrawal from the account before the legal conditions are met. Early withdrawal shall incur penalties that are calculated proportionate to a unit-holder's time from first contribution to withdrawal.	Yes, Article 104, 30% of collected amount before its reduction for fees.	Yes, it is obligatory if the accumulated amount on the account is less than KM 2000.	Yes, according to article 12, payment can be made in the form of a lump sum or transfer to the Individual Account of the Beneficiary. Article 14 specifies that a Defined Contribution Pension Fund shall provide for payment of benefits in the form of Annuities in accordance with the provisions of this Law pertaining to Savings Pensions or for payment in installments or in a lump sum, at the option of the Participant.	No, article 89[8]. However, article 92 stipulates (1) When a Member of a mandatory pension fund is not entitled to an old age pension because he/she has not completed at least 15 years of pension service, he/she can buy a monthly pension annuity if that amount is equal or higher than 40% of the minimum pension. (2) When the calculated amount of the pension annuity is less than 40% of the minimum pension, the mandatory pension fund shall pay to the member a lump sum equal to the accumulated amount on his/her account. (3) Purchase of pension annuity and payment of accumulated amounts, may be done after the age of 65.	Yes, up to 30% of the fund paid in cash and remainder in monthly or periodic installments not later than 3 years from the date of withdrawal from the fund	Article 62 stipulates that pooled funds may be withdrawn as a lump-sum payment, scheduled payment, used for a purchase of annuities, or in a combination thereof. A voluntary pension fund member may withdraw at most 30% of pooled funds as a lump-sum payment.

Tax treatment	The employer and employee contributions to the pension fund schemes are recognized as non-taxable income, up to the legal limits. Details in articles 88 and 89.	The tax treatment of voluntary pension contributions, determined in the draft Personal Income Tax Law pending in the Federation B&H Parliament, has not yet been enacted.	Employers are exempt from payment of the company income tax and contributions for pension insurance on the gross salaries of their employees, if they pay annually up to a maximum of BAM 1,200 (€ 613) in the European Voluntary Pension Fund.	The Law on Pension Funds of Kosovo (article 37): Contributions made by an employer to KPST or an additional pension fund for the benefit of its employees is deemed an operating expense and reduces the operating result of the employer subject to earnings tax. Contributions by an employee to KPST or in an additional pension fund, is exempt from personal income tax.	Annual incentive to the amount of four average gross wages in the previous year through returning of paid personal or company income tax (€2136)	No deduction or exemption	Employees and employers can save up since contributions from employer's funds up to RSD 5,757 (€ 50) per employee per month are exempt from the personal income tax and contribution for mandatory social insurance.
Other indicators and comments	The Raiffeisen Prestige Investment Fund has 87.7% in the total capital of all pension funds' investment portfolio.	The public awareness about the opportunities for voluntary pension savings in the Federation B&H and the benefits of doing so is exceptionally low.	In the period from establishing in 2017 until February 2019, the first eight beneficiaries received pensions from the European Voluntary Pension Fund.	The case of Kosovo has been unique given that it did not inherit any system or any funds for retirement age. Thus, there is the three-pillar system.	Some well-judged regulatory intervention has ensured progressive reductions in fee levels- Investment returns have been relatively good for a young system facing initial set up costs and a financial crisis early in its development.	Montenegro is a rare example of a country providing no financial incentives or tax exemption or deduction for investing in voluntary pension funds.	Serbia has a high concentration in the voluntary pension funds market

1 For the detail regarding the Voluntary Fund Fees, see national report for Republic Srpska

2 Source: capital.ba, 2019. Do kraja godine oko 9.000 članova dobrovoljnog penzijskog fonda u RS, 6 January 2019, available on https://www.capital.ba/do-kraja-godine-oko-9-000-clanova-dobrovoljnog-penzijskog-fonda-u-rs/

3 Evropski dobrovoljni penzijski fond, 2019b. *Vrijednost neto imovine fonda*, available on https://www.epf.ba/dobrovoljni-penzijski-fond/postojeci-clanovi/vrijednost-neto-imovine-fonda

4 According to the Labor Force Survey, exact number of employees in 2013 was 338,364. Agencija za Statististiku Kosova Odeljenje za Socijalnu Statistiku Sektor tržišta rada, 2014. *Anketa o radnoj snazi: rezultati za Kosovo 2013*, Priština: Agencija za Statistiku Kosova, available on http://documents.worldbank.org/curated/en/658641468336310613/pdf/929120REVISED00vey02013000SRB000WEB.pdf

5 Data for Kosovo GDP are taken from https://tradingeconomics.com/kosovo/gdp-constant-prices

6 Source: Atlaspenzija, 2019. *Najčešća pitanja*, available on http://www.atlaspenzija.me/main.php?idstr=73

7 Data for the North Macedonia GDP are taken from

8 Source: Agency for Supervision of Fully Funded Pension Insurance (MAPAS), 2019a. *Monthly Bulletin 03.2019*, Skopje: Agency for Supervision of Fully Funded Pension Insurance, available on http://mapas.mk/wp-content/uploads/2019/04/Bilten-03-2019.pdf

9 Law on mandatory fully funded pension insurance by the Republic of Macedonia.

Sources: various national documents mentioned in the report, particularly for RoR: OECD, 2018a. Table A.4. Nominal annual net investment rates of return of funded and private pension arrangements (%), 2007-2017.

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KAPITALIZIRANO MIROVINSKO OSIGURANJE U ŠEST BALKANSKIH ZEMALJA KOJE NISU ČLANICE EU

Sažetak

Cilj ovog rada je pružiti pregled stanja kapitaliziranog mirovinskog osiguranja u šest zemalja na Balkanskom poluotoku: Albaniji, Bosni i Hercegovini, Kosovu, Crnoj Gori, Srbiji i Republici Sjevernoj Makedoniji. Promatrane zemlje iz različitih razloga, osim Kosova i Republike Sjeverne Makedonije, nisu prihvatile obvezno i dobrovoljno kapitalizirano mirovinsko osiguranje. Iako postoje brojne prednosti privatnog kapitaliziranog mirovinskog osiguranja - prije svega diversifikacija rizika, bolja zaštita od političkih pritisaka i mogućnost razvoja financijskog tržišta, postoje i istraživanja koja pokazuju relativno slabe pozitivne učinke takvog sustava. Mirovinski fondovi u promatranim zemljama suočavaju se s važnim izazovima u vezi s raspodjelom i ulaganjima postojeće imovine. Državni vrijednosni papiri i bankarski depoziti i dalje predstavljaju veliki dio portfelja mirovinskih fondova. Proces učinkovite podjele privatnoga financijskog rizika može se znatno ubrzati pripremama za članstvo u EU.

Ključne riječi: Kapitalizirani mirovinski sustav, mirovinska reforma, Balkanske zemlje.

JEL klasifikacija: G23, H55.