PRIVATIZATION OF PENSIONS – THE NIGERIAN EXPERIENCE

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BACKGROUND

- Prior to the Pension Reform Act 2004 (PRA), the Nigeria Pension system had the following characteristics:

- Huge pension deficits: Pension Deficits for the Federal Civil Service as at 2005 was calculated to be about $9.3billion while we estimated the Pension liability for the 36 states to be $14.7billion

- Unsustainable pay-as-you-go system: The Public Service operated an unfunded Defined Benefits Scheme and the payment of retirement benefits were budgeted annually
- Poor pension administrative structures

BACKGROUND

- Weak and fractured regulatory regime.
- The outcome of the reform was the enactment of the Pension Reform Act 2004
- The Act provided a chance to start on a new slate and took a cursory review of supervisory structures and trends around the world.

RATIONALE & OBJECTIVES OF PENSION REFORM

Rationale for reforms:

- Most schemes were underfunded or unfunded.
- Unsustainable outstanding pension liabilities.
- Weak and inefficient pension administration.
- Scheme not regulated.

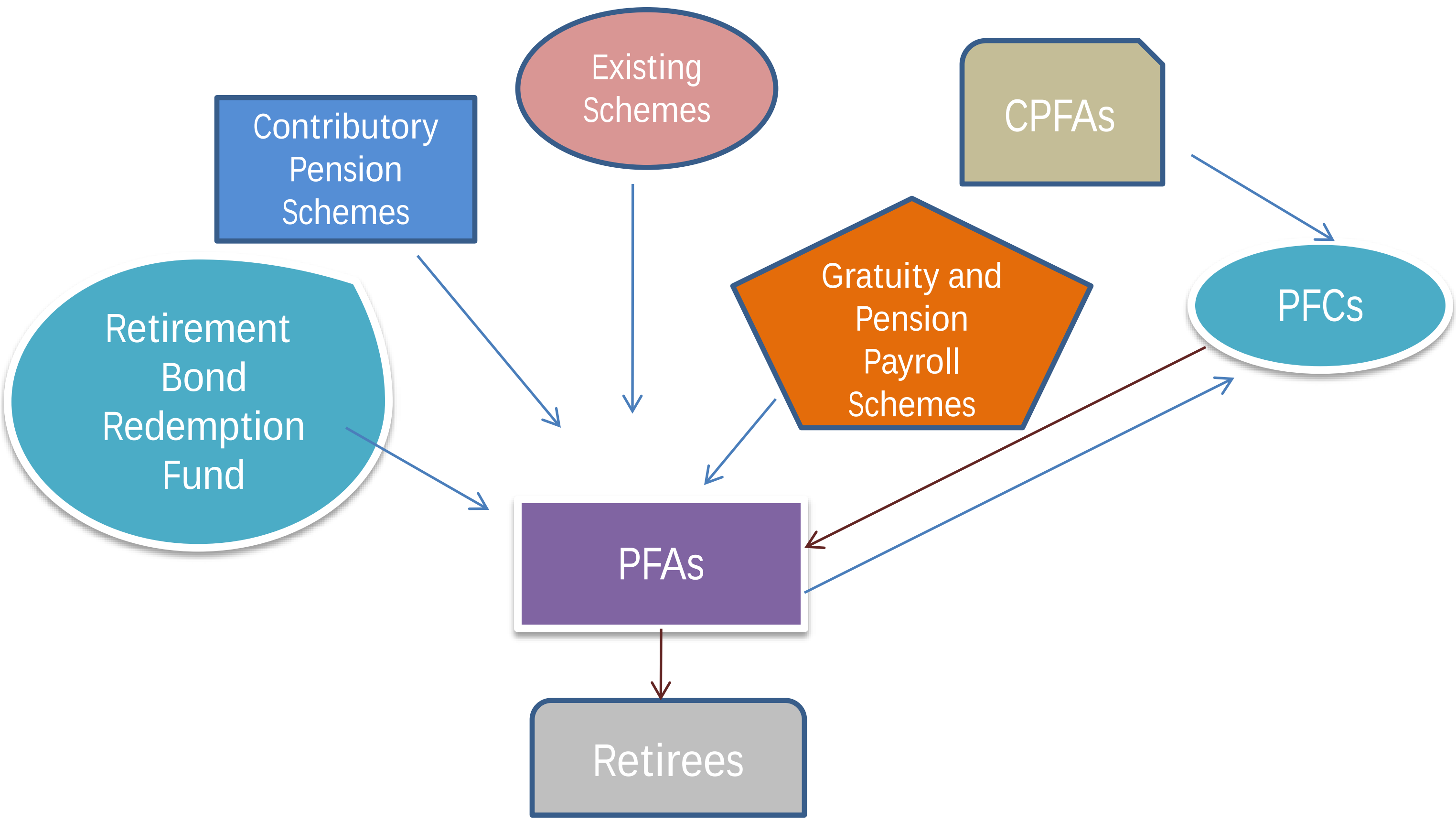
Reform objectives:

- Ensure that every worker receives his retirement benefits as and when due and stem the growth of pension liabilities.
- Empower the worker and assist workers to save in order to cater for livelihood during old age.
- Establish uniform rules, regulations and standards for administration of pension matters.
- Secure compliance and promote wider coverage.

NATIONAL PENSION COMMISSION

- Apex body to regulate and supervise pension schemes
- Formulate, direct and oversee the overall policy on pension matters in Nigeria
- Approve license and supervise Pension Fund Administrators (PFA), Pension Fund Custodians (PFC) and other institutions relating to pension matters
- Maintain National Data Bank on pension matters
- Receive and investigate complaints against any PFC, PFA and Employer

STRUCTURE OF THE NEW NIGERIAN PENSION SYSTEM



ELEMENTS OF THE CONTRIBUTORY SCHEME

- **Fully Funded**: The contributions are deducted immediately from the salary of the employee and transferred to the relevant retirement savings account.
- **Individual Accounts** : The employee opens an account to be known as a ‘**Retirement Savings Account** in his name with a Pension Fund Administrator of his choice
- **Transparency** : The PFAs are separate from the PFCs.
- **Security**: **Life Insurance Policy:** Every employer shall maintain life insurance Policy in favour of an employee for a minimum of three times the annual total emolument of the employee
- Strict Investment Policy

COMPARING THE OLD AND THE NEW SCHEMES

	Old Scheme	New Scheme
Type	Largely Defined Benefit	Largely Defined Contribution
Funding	Mostly unfunded & PAYG	Contributory & Fully Funded
Pension Portability	Not Portable	Personalised & very portable
Supervision	Fragmented & Unregulated (SEC, NAICOM, JTB)	Strictly regulated by Pencom
Pension Liabilities	Implicit & not transparent	Explicit through retirement benefits bond
Tax Exemption	Limited	Contribution & retirement benefits
Dismissal from Service	No Pension Benefits	Full Pension Rights
Insurance Policy	Voluntary and mostly in private sector	Mandatory for all employers.

TRANSITION CHALLENGES

- General misconception and knowledge gap about the new scheme
- Widening coverage especially in the informal businesses in the private sector
- Registration of contributors - lack of reliable identification instrument, incomplete documentation
- Enforcement in the private sector

  -Mostly informal

  -Difficult to locate address

  -Inadequate records
- Determining the total accrued pension liabilities and funding the shortfalls in pension assets in the private sector

PENSION REFORM IMPLEMENTATION EFFORTS

- Issued Guidelines and Regulations
- Licensing 26 PFAs, 7 CPFAs ad 5 PFCs
- Approved the continuation of 18 Existing schemes.
- Registered about 4,012,000 RSA Contributors as at December 2009.
- 26,000 registered members of CPFAs
- 41,500 registered members of Approved Existing Schemes.
- Total Pension Fund Assets $7.33 Billion as at 31st December 2008 and $9.6 billion as at December 2009.

PENSION REFORM IMPLEMENTATION EFFORTS

- As at December, 2007 the PFAs had only about 34% of assets under management
- Computation of accrued benefits of current employees of the Federal Government of Nigeria (FGN) was carried out and issuance of retirement benefits bonds had commenced.
- About US$2.5billion has been paid to verified pensioners of FGN as at December 2009.

CURRENT STATE OF PENSIONS IN NIGERIA

Nigeria – Demography

Age Band	Male	Female	Total	%
0-14	31,624,050	30,242,637	61,866,687	41
15-64	42,240,641	40,566,672	82,807,313	55
65 Years and over	2,211,840	2,343,250	4,555,090	4
Total Population	76,076,531	73,152,559	149,229,090	100

Population : Growth Rate: 2%
Labor Force: 51 million

CURRENT STATE OF PENSIONS IN NIGERIA

Growth Rates

Period	Annualized Growth rate in membership (%)	Annualized Growth rate of AUM (%)
Oct 06-Dec 07	80	30
Dec 07-Dec 08	24	35
Dec 08- Dec 09	18	31
Average annual Growth (Oct 06-Dec 09)	40	32

Period	Registered Members	AUM ($ billions)
Oct 06	1,400,000	4
Dec 07	2,784,273	5.4
Dec 08	3,465,764	7.3
Dec 09	4,080,000	9.6

Total growth in membership-191%
Growth Rate of Assets under Management – 140%

CURRENT STATE OF PENSIONS IN NIGERIA

- **MARKET SHARE BY ASSETS UNDER MANAGEMENT**

Group	Individual Holding	Market Share (%)
Top 5 Operators	5%+	60%
Top 10 Operators	3%+	82%
Top 15 Operators	1%+	94%
Top 20 Operators	0.4%+	98%

- 20% of PFAs control 60% of the market
- 40% of PFAs control 82% of the market
- 60% of PFAs control 94% of the market

COMPOSITION OF PENSION FUND PORTFOLIO (2007-2009)

Asset Classes	2007 (%)	2008 (%)	2009 (%)	Pencom Investment Limits
Ordinary Shares	29.6	17.02	13.78	25%
Govt. Securities	34.3	37.08	37.6	100% (FGN), 30% (STATE)
Corporate Debt Securities	0.03	1.36	1.44	30%
Money Market Securities	19.63	33.46	33.99	35%
Open/Close-End Funds	0.54	0.51	0.31	5%
Real Estate Property	9.7	8.99	10.01	As approved by the commission
Others	6.2	1.58	0.2	As approved by the commission
Total	100	100	100	

COMPOSITION OF PENSION FUND PORTFOLIO (2007-2009)

- Number of listed companies on the floor of stock exchange – 215
- Market capitalization of top 20 companies- $26bn

LESSONS FROM CHILE

- **Chile- Demography**

Age Band	Male	Female	Total	%
0-14	1,966,017	1,877,963	3,843,980	23
15-64	5,625,963	5,628,146	11,254,109	68
65 years and Over	627,746	875,872	1,503,618	9
Total Population	8,219,726	8,381,981	16,601,707	100

Population: Growth rate:0.881%
Labor Force:7.3 million

THE CHILEAN EXPERIENCE

- The new system was perceived as a model for many countries in Latin America and for emerging economies elsewhere.
- The privately managed accounts currently covers 60% of workers–a percentage greater than privately managed pension systems in other countries
- When the AFP system was created in 1981, only 12 AFPs existed
- By 1999 the number had increased to 21. However, after an intense process of acquisitions, mergers, fusion and transnationalization, only 5 AFPs exist today.

THE CHILEAN EXPERIENCE

- The AFP with the largest market share had 30.4% of assets under management
- 40% of the AFPs had 56% of assets under management
- 60% of AFPs had 78% of assets under management

SUMMARY OF THE EVOLUTION OF PRIVATE PENSIONS IN CHILE

	1981	2000	2009
Total contributors	1.06m	3.2m	4.3
Number of AFPs	12	21	5
Fund Assets	$236m	$32bn	$102bn

FUTURE PROSPECTS FOR NIGERIA

- Current annual contributions into the scheme is $1.05bn
- Current annual pay out from the scheme is $26.5m
- After 28 years, the number of contributors to the pension scheme in Chile is 60% of its labour force.
- Drawing from that experience, assuming we follow the same trend, Nigeria will be expected to have about 60% of its labour force as contributors to the pension scheme in 28 years.
- Therefore total contributors is estimated to be about 31.2m by the year 2034

FUTURE PROSPECTS FOR NIGERIA

YEAR	CONTRIBUTORS	FUND ASSETS (US$)	ASSET MGT FEES (US$)	ADMIN FEES (US$)	CUSTODIAN FEES (US$)	No of PFAs	No of PFCs
2006	1.4m	4bn	66m	11.2m	43.5m	13	4
2009	4.08m	9.6bn	139.2m	31.2m	34.8m	26	5
2011	6.2m	35.6bn	540.5m	48.5m	134.1m	??	??
2016	11.7m	86.0bn	414.7m	45.9m	82.9m	??	??
2021	17.1m	176.8bn	858.5m	67.6m	171.7m	??	??
2026	22.5m	335.8bn	1.6bn	89.3m	327.2m	??	??
2031	27.9m	608.1bn	2.9bn	110.9m	593.7m	??	??
2034	31.2m	855.1bn	4.2bn	124m	835.3m	??	??

FUTURE PROSPECTS FOR NIGERIA

- PFA : not more than 10 will be in the market in 10 years time
- PFC: not more than 2 will be in the market in 10 years time
- New investment products because of limited outlets
- Deepening of the bonds market
- Corporate bonds
- Annuity products to compete with programmed withdrawals
- IFPM Projections
- Greater actuarial involvement in the evolution of the industry

EVALUATION OF PRIVATE PENSIONS IN NIGERIA

Private pension scheme in Nigeria still faces a number of challenges among which are:

- Misconceptions and apprehensions about the scheme. Although this has reduced when compared to inception.
- Coverage would have to be expanded how to cover the informal sector that has over 60% of total labour force
- Capacity building in the industry to address the general knowledge gap, especially on pension administration
- Encouraging State and Local Governments to adopt the Contributory Pension Scheme
- Inadequate investment outlets to absorb growth of savings.

EVALUATION OF PRIVATE PENSIONS IN NIGERIA

However ,

- There is still a huge growth opportunity
- Federal government has consistently met its obligations
- There is now a harmonized defined contributory scheme in the public and private sector.
- Huge pension deficits which had hitherto been a problem have been eradicated as the current scheme is fully funded
- Effective and efficient regulator
- Buildup of huge long term funds

EVALUATION OF PRIVATE PENSIONS IN NIGERIA

- Expected growth in annuity market
- Huge group life insurance market
- Individuals are now able to save up for retirement
- Portability of RSA will lead to good retirement

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