Will You Afford to Retire?

The Real Return on Long-Term and Pension Savings

2024 Edition

BETTER FINANCE

The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

Will You Afford to Retire?

The Real Return of Long-term and Pension Savings

2024 Edition — Romania

A research report by BETTER FINANCE

COORDINATORS

Sébastien Commain
Ján Šebo

CONTRIBUTORS

Sara Álvarez
Sébastien Commain
Daniela Danková
Laetitia Gabaut
Lisbeth Grænge Hansen
Christian Gülich
Amadeus Malisa
Guillaume Prache
Joanna Rutecka Góra
Ján Šebo
Thomas Url

REVIEWERS

Sara Álvarez
Sébastien Commain
Aleksandra Mączyńska
Ján Šebo
Rina Zhubi

Disclaimer

This report is an independent research publication, elaborated through the efforts of its independent coordinators, contributors, and reviewers.

The data published in this report stems from publicly available sources (national statistics institutes, regulatory bodies, international organisations etc) which are disclosed throughout the report.

The authors and contributors produce and/or update the contents of this report in good faith, undertaking all efforts to ensure that there are no inaccuracies, mistakes, or factual misrepresentations of the topic covered.

Since the first edition in 2013, and on an ongoing basis, BETTER FINANCE invites all interested parties to submit proposals and/or data wherever they believe that the gathered publicly available data is incomplete or incorrect to the email address policy@betterfinance.eu.

Download the full report:

https://betterfinance.eu/publication/will-you-afford-to-retire-2024

Executive Summary

Was 2023 the year when European retail investors finally obtain the "fairer deal" that the outgoing European Commissioner Mairead McGuiness wished for them (McGuinness, 2023)? As far as long-term and pension products are concerned, this report presents mixed results. While European capital markets performed strongly in 2023, helping many pension funds and life insurance companies to rebound after a calamitous 2022, we find that many of the products we analyse failed to pass on the benefits of this renewed performance to pension savers. One or even two years of past performance, however, do not tell us much about the long-term performance of saving products. What matters for individuals who invest part of their income into those products is how much income they will be able draw from them in the distant future, in particular for retirement purposes. The objective of this report therefore is to provide readers with a long-term perspective on performance that aligns with the extended investment horizon. We analyse the costs and performance of a broad range of products across various holding periods, spanning up to 24 years. Over this longer period good years supposedly make up for bad ones. Nevertheless, we observe that many of the product categories do not offer sufficient nominal returns in the long run to compensate for inflation, even with the moderate inflation rates of the of the 2000s and 2010s. This weak performance then results in a loss of purchasing power for many European savers and investors.

The real net return of European long-term and pension savings

The object of this report is to assess the ability of long-term and pension savings products to at least preserve the purchasing power of European retail investors' savings over more than two decades, and at best increase the real value of these savings, increasing the capital on which European pension savers may rely on to maintain their living standard in retirement. That is why we focus our analysis on time-weighted returns.

The risk of financial losses is inherent in any investment in capital markets: capital markets are volatile—as their performance over the last two years clearly shows (see Figure XS.4). Nevertheless, we share European Insurance and Occupational Pensions Authority (EIOPA)'s view that

> the riskiness of a personal pension product is its potential inability to outperform inflation, and so to lose savings in real terms, or not being sufficiently "aggressive" to reach higher investment returns to compensate for potentially low contribution levels (European Insurance and Occupational Pensions Authority [EIOPA], 2020, p. 3),

and generalise it to any long-term and pension savings product. Short-term volatility—the alternance of good and bad years—is of little consequence for most pension savers; what matters is the cumulated performance over the life of the contract, the holding period, which often spans more than two decades. Over such long periods, the crucial risks are those arising from cumulated costs—which divert a portion of the accumulated capital towards financial intermediaries profit and loss accounts—and inflation—which progressively erodes the purchasing power of savings. The *real net rate of return* is therefore the main metric of interest for pension savers.

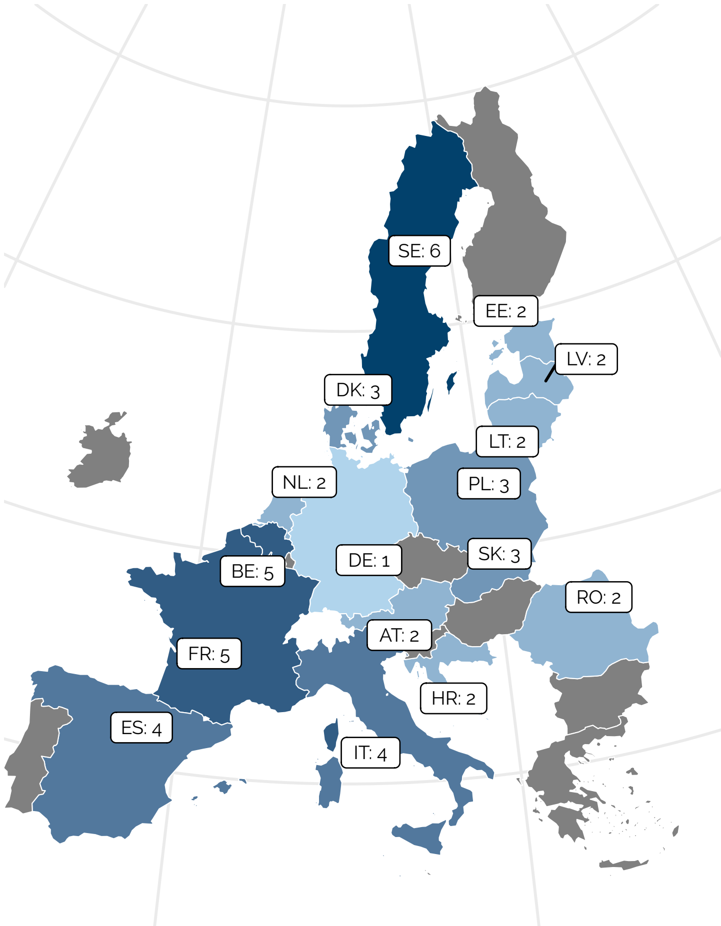
This research report by BETTER FINANCE covers 16 of the 27 European Union (EU) Member States. In each of these countries the team of contributors analyses the costs and performance of up to 6 product categories. Our goal is to calculate, based on publicly available data about these product categories, the *real net return* that long-term and pension savers may expect to obtain from their investments, going back as far as the year 2000. When we refer to real net return, we are indicating the rate of return on an investment after deducting all costs and charges levied by the product provider. This calculation also accounts for inflation, which reduces the purchasing power of both the invested capital and returns. The map in Figure XS.1 shows the countries included in this study, and the total number of product categories analysed in each country.

Assessing the real net return of a category of pensions products requires three classes of information about these products: (a) reliable data about the nominal, gross return of investments made on behalf of pension savers in relation to the total amount of accumulated capital; (b) total costs being levied for the management of these investments (administrative costs of managing the investor's contract, cost of management of investment fund "units", entry fees, exit fees, etc.) and; (c) the rate of inflation in one's country for each year of the investment period.

These are but typical examples of the data availability issues that our team of expert contributors face across countries and product categories. While data about average inflation is easy to come by—thanks, inter alia, to the work of Eurostat—, we can hardly say the same for data about returns and costs. The availability of such data often limits the scope of our study. Reliable information about the average performance of a product category may be unavailable, as is the case of most German long-term and pension saving products, or not fully appropriate for an assessment of what the client actually get, as is the case with Belgium's *Assurance Groupe* products. Costs data are even more difficult to obtain: for many of the product categories we analyse, cost information is too scarce to assess the impact of costs on performance.

Long-time followers of BETTER FINANCE's work on pensions might remember that past editions of the report also included Bulgarian pensions products and may be surprised to see that we analyse no product category in Bulgaria in this report. In the case of Bulgaria, despite BETTER FINANCE's multiple calls to the relevant authorities, essential data necessary to calculate the real net returns of Bulgarian pension savings remain unavailable, forcing us to renounce including any Bulgarian long-term or pension savings product category in our study.

Figure XS.1 – Countries and number of product categories included in the report

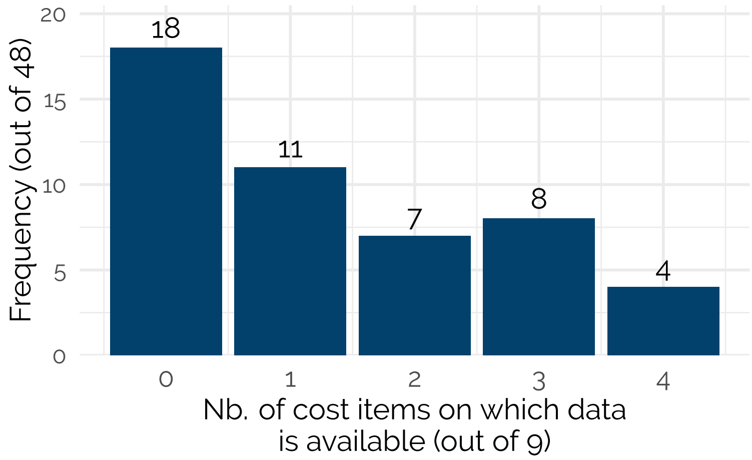


Besides performance data, information on costs is very often patchy and displayed in a way that makes it impossible for investors to compare cost levels across product providers, and for our contributors to aggregate this information at the level of product categories. The reader can appreciate this reality in Figure XS.2: for none of the 48 product categories included in our study could our contributors find data for more than 4 out of the 9 cost items defined in our methodology. Additionally, for more than a third of the product categories in our study, there is simply no cost information available.

For the 18 product categories for which no cost data is available, the lack of information on costs and charges prevents us from evaluating the average effect of charges on investors' returns. Consequently, we are forced to start our analysis with disclosed nominal *net* returns, whereas providers' marketing communications usually communicate on the basis of nominal *gross* returns.

Given the challenges in obtaining fundamental data on the average costs and performance of long-term and pension savings products, which capture a large share

Figure XS.2 – **Availability of cost and charges data for 2023**



of the wealth of European households, we advocate for EU and national authorities to urgently enact and implement the proposed rules on product oversight, governance, and information to investors, as outlined in the recent Retail Investment Strategy (RIS) proposals made by the European Commission (see our policy recommendations on Page xiii). Costs and performance disclosures are key to properly assess the functioning of the European market for pension savings products.

While opacity on cost and charges presents a challenge for many of the product categories we study, it is only fair to acknowledge the few cases in which industry and supervisors made significant efforts to define and implement coherent reporting frameworks, such as that of the Dutch pension funds or the Italian *Commissione di Vigilanza sui Fondi Pensione* (COVIP)'s annual report on pension funds and *Piani Individuali Pensionistici* (PIP).

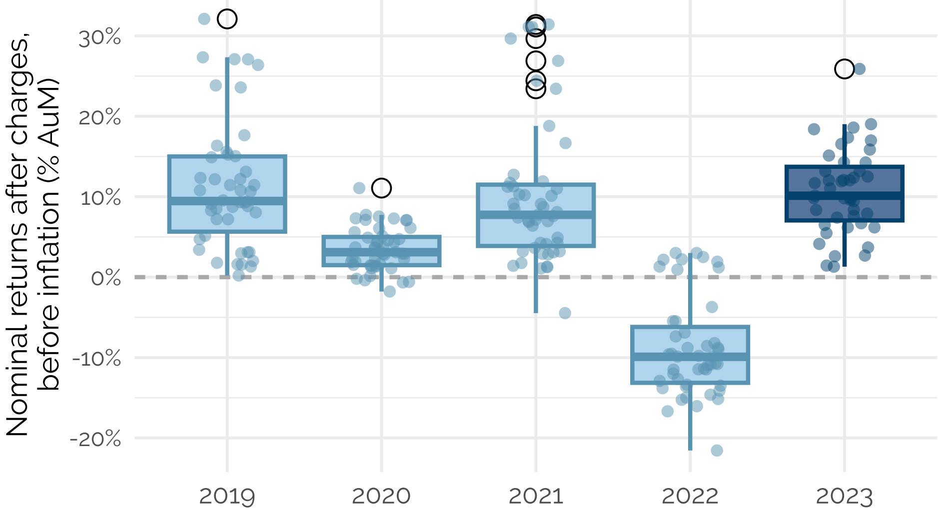
2023: Recovering from the slump

The product categories included in our study generally performed strongly in 2023. All of the 43 product categories for which we could obtain performance data for 2023 had a positive nominal net return. As can be appreciated in Figure XS.3, this performance is in sharp contrast with the previous year, when out of 47 product categories, 38 returned a loss in nominal terms, after charges.[1]

These good results reflect the good performance of, in particular, equity markets between January and December 2023, which recovered strongly after the slump of 2022. Figure XS.4 shows the performance of European capital markets. Using two pan-European market indices as proxies—one for equities and one for bonds, we calculate the cumulative return of a hypothetical portfolio composed of European equity and bonds in equal proportion, with annual rebalancing. The cumulated return, in nominal terms, of this portfolio dropped by 44.8 percentage points between

[1]In box plots such as Figure XS.3, the central box represents the interquartile range (i.e., 50% of the data), the thick central line is the median, the whiskers (vertical lines) indicate where roughly 99% of the data points are located, and the black circles at each end of the whiskers represent outliers.

Figure XS.3 – **Average 1-year return rates of analysed product categories (2019–2023)**



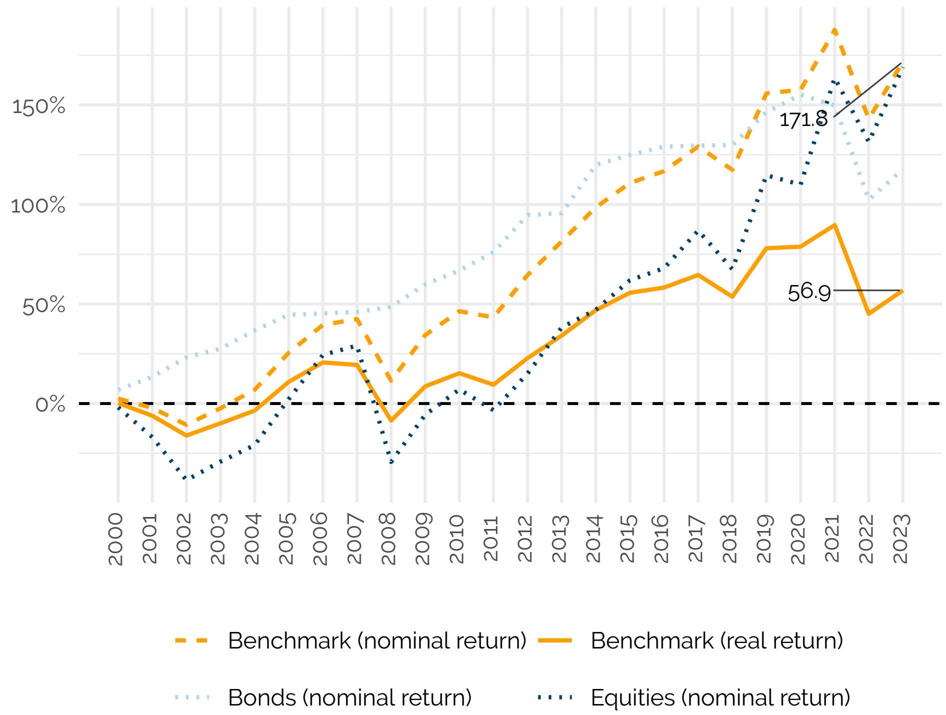
Data: NCAs and sectoral associations (see Country Cases); *Calculations:* BETTER FINANC

end-2021 and end-2022 before rebounding to 171.8% by the end of 2023. After adjusting for the average inflation across the EU, we obtain a 56.9% real net return, +11.8 percentage points (p.p.) from end-2022.

Inflation, in turn, slowed down in most EU countries in 2023, after the peak of 2022. In 8 of the 16 countries of our study, inflation in 2023 was below the annual average over the period 2000–2003. Nevertheless, for most of our sample, inflation remained high, as can be observed in Figure XS.5. Inflation across the Euro Area, stood at 2.93%, still significantly above the close-to-but-below-2% target of the European Central Bank (ECB).

The result of this combination of strong capital market performance and slowing inflation is a reduced gap between nominal net returns and real net returns for 2023: With a median net return standing at 10.1% in nominal terms and 7.4% after inflation, the gap is reduced to 2.8 p.p. (see Figure XS.6), down from 8.6 p.p. in 2022, when the already severly negative median nominal returns (-9.9%) where further depressed by the strongest inflation seen in Europe is decades, yielding a median real net return of -18.5%. These median values, it should be noted, hide markedly contrasting differences: The maximum performance for 2023, in nominal terms and after deduction of charges, stands at +25.9% (Poland's Employee Capital Plans), while the poorest performance with +1.3% (ironically, that of Italian PIP "with profits" contracts) narrowly avoids returning a loss in real terms thanks to the low level of inflation in Italy (+0.46%).

Figure XS.4 – **Cumulated performance of European capital markets (2000–2023)**



Pan-European Pension Product (PEPP): First full year of return data

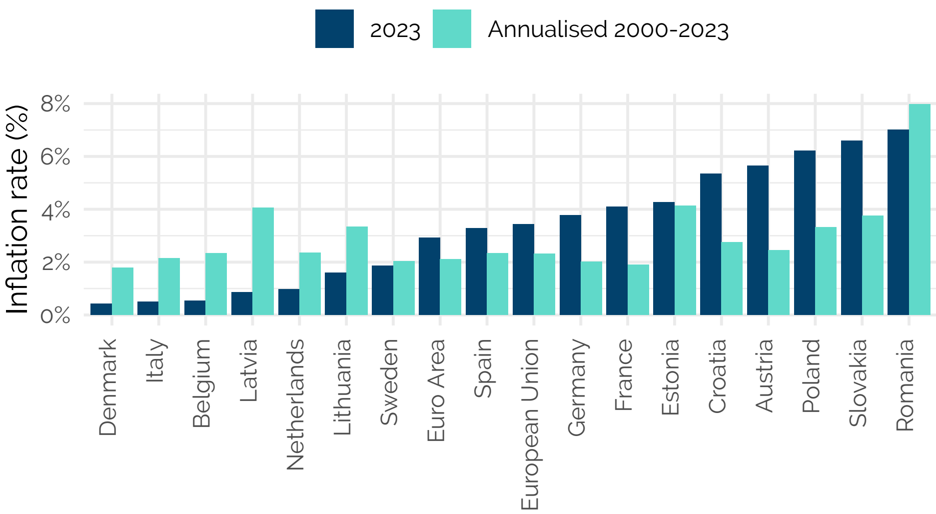
We wish to highlight the good performance of the first PEPP to be included in our study: with a nominal return before charges and inflation standing at +15% and charges amounting to 0.72% of assets under management (AuM), the Slovak PEPP yielded a net return of +14.3% in nominal terms and 7.2% in real terms, largely outperforming its capital markets benchmard (11.8% and 4.9% in nominal and real terms, respectively). Find more information in the Slovak country case in part II of this report.

These data show that the PEPP is indeed a promising personal pension product. The Slovak case shows that it is indeed possible to offer a PEPP under the conditions set by the current PEPP regulation, including the "1% fee cap", that is, the limiting of fees to 1% of accumulated capital per annuum for the Basic PEPP.

BETTER FINANCE will keep monitoring its development not only in Slovakia, but also in Poland—another of the country cases of this report, where PEPP was introduced in the course of the year 2023—and other countries.

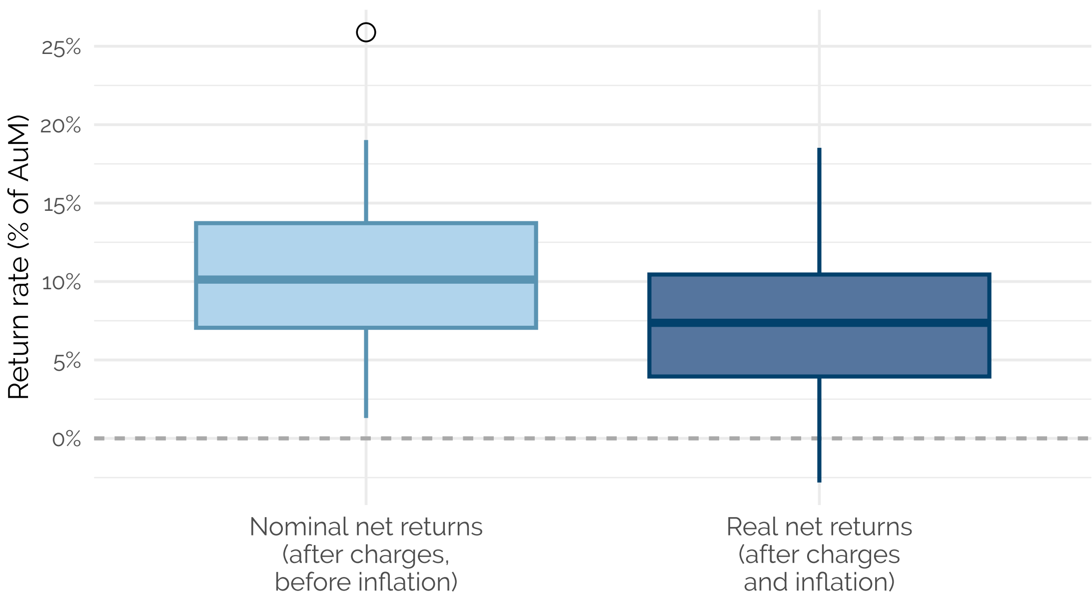
In the meantime, we urge Member State governments to offer the PEPP the same treatment, as regards taxation, subsidies and transferability of accrued pension benefits, that existing national personal pension products enjoy (see our policy recommendation on this topic on Page xvii).

Figure XS.5 – **Inflation 2023 vs. 2000–2023 annual average**



Data: Eurostat (HICP monthly index); *Calculations:* BETTER FINANCE.

Figure XS.6 – **Average 1-year nominal vs. real return in 2023 (after charges, % of AuM)**

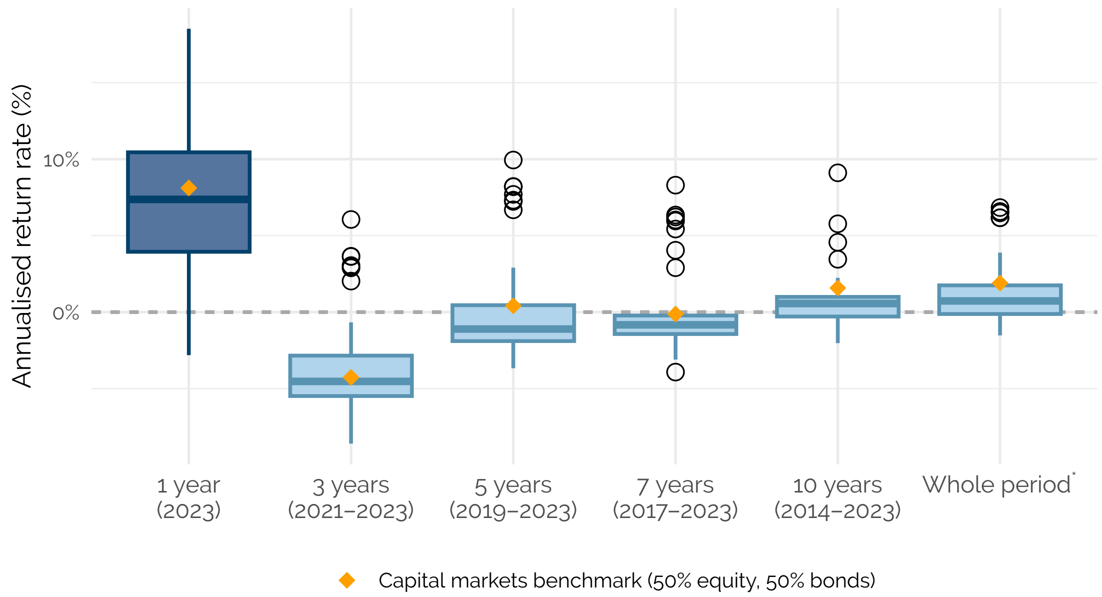


Calculations: BETTER FINANCE

The long-term view on long-term savings

Naturally, one should not assess the performance of long-term and pension savings products based on the results obtained in one bad year but rather take a long-term view. That is why our ambition in this report is to gather data about costs and performance for a period of up to 24 years (2000–2023).

Figure XS.7 – Average annualised real net returns over varying holding periods



Calculations: BETTER FINANCE; * Up to 24 years, the reporting period varies across products

Figure XS.7 displays the distribution of average performances after charges and inflation of the long-term and pension saving products analysed in our report, over varying holding periods from 1 year (2023) to the whole period for which data could be found ("whole period", up to 24 years). We immediately observe that the capital markets slump of 2022 still weighs down on performance over shorter periods (3, 5 and even 7 years), with annualised rates after charges and inflation negative for a large majority of product categories. Over 7 years (2017–2023), the negative performance of 2022 comes atop that of the year 2018, with the result that only a few outliers manage to yield a positive real net return over that period.

Market volatility, whether upwards or downwards, is cancelled out over longer periods (the standard devaition falls from 4.9 p.p. for 1 year to 2 p.p. for 10 years, see Table XS.1), allowing us to more accurately assess the returns offered by the various product categories. Over 10 years and over whole reporting periods (up to 24 years), we see that the most of the interquartile range (the boxes in Figure XS.7) lies in positive territory. This may seem reassuring, until one notes that over 7 years, 10 years and whole periods, the annualised real performance of our capital markets benchmark (50% equity–50% bonds, rebalanced annually), shown with a yellow diamond in the figure, lies in the top quartile of the returns of product categories (above the upper bound of the box), meaning that 75% of the product categories fail to beat the benchmark.

Table XS.1 – Summary statistics of real performance over varying holding periods

Holding period	Nb. of product cat.	Median	Mean	Standard Devia-tion	Best perfor-mance	Worst perfor-mance
1 year	43	7.4%	7.3%	4.9pp.	18.5%	-2.8%
3 years	47	-4.5%	-3.6%	3.4pp.	6.1%	-8.6%
5 years	46	-1.1%	0.2%	3.5pp.	9.9%	-3.7%
7 years	46	-0.8%	0.0%	2.8pp.	8.3%	-3.9%
10 years	40	0.6%	0.7%	2.0pp.	9.1%	-2.0%
Whole period*	48	0.8%	1.3%	2.3pp.	7.2%	-1.5%

Calculations: BETTER FINANCE

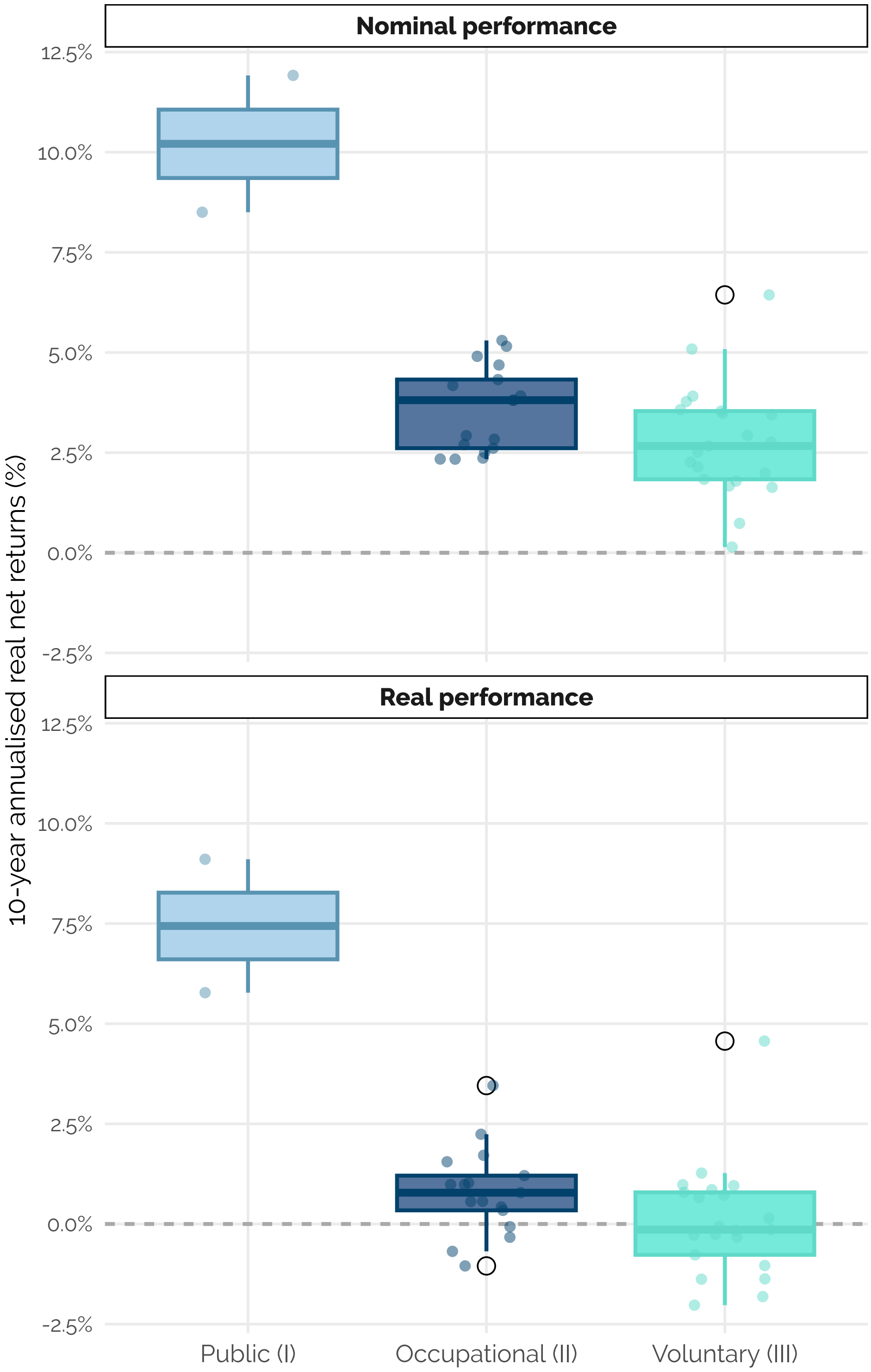
* Whole period varies across products (up to 24 years).

Observing the distribution of performance levels across pension system pillars, we also note that occupational pension schemes in Pillar II generally outperform voluntary products within Pillar III. Figure XS.8 illustrates the distribution of 10-year performance per pillar.

Swedish Premium pensions, which show very strong performance compared to the rest of the analysed product categories, are classified as Pillar I but although they are funded, earnings-based pensions that bear strong resemblance to occupational pension schemes (Pillar II). Leaving these extreme positive outliers aside, we observe that median 10-year performance of Pillar II products (central line of the middle box) is above the upper limit of the interquartile range of Pillar III performances (upper bound of the right-hand box), meaning that 75% of Pillar III products have a performance below the median performance of Pillar II products.

It is beyond the scope of this report to explore the significance of the trend, although future research should investigate the factors that may explain it, including differences in asset allocation, management costs, distribution costs, and the potential effect of auto-enrolment schemes. Additional cost data would be particularly valuable to consistently analyse whether the observed divergence in performance might arise from higher costs associated with Pillar III products. We hope that such data becomes available if the EU legislator follows the much-welcomed proposals regarding cost disclosures under the Markets in Financial Instruments Directive (MiFID) and Insurance Distribution Directive (IDD), crucial elements of the European Commission's proposals for the Retail Investment Strategy (RIS).

Figure XS.8 – **Average 10-year annualised performance per Pillar**



Calculations: BETTER FINANCE, returns are shown after charges and inflation.

Policy recommendations

Policy recommendation 1 — Supervisory reporting and statistics

Step up efforts to collect and disclose data on long-term and pension savings products, both at the national and EU level (ESAs's cost and past performance reports) to empower European citizens as retail investors.

The contributors to this report can testify of the difficult to obtain even basic, aggregated data about long-term and pension products in many EU countries. If a team of expert contributors, with knowledge and experience in the field, find it challenging, how can we expect EU citizens to make any use of these data to assess the performance of their own pension products in relation to the market? Making available full historical data sets of both aggregated and provider-level data would enable non-profit organisations like BETTER FINANCE to provide an independent, consumer-friendly analysis of this market. But national competent authorities (NCAs) could also step up their efforts to create consumer-friendly reports and comparison tools.

Harmonised frameworks for reporting from product providers to NCAs and pension scheme participants already exist for various of the product categories we analyse in this report. These commendable efforts should be assessed through a peer-review process to be organised by the European supervisory agencies (ESAs) in order to identify best practices, but also discard misleading disclosure practices that prevent retail investors to obtain a clear picture of the cost and performance of the products on offer. As part of these efforts to better report on the costs and performance of retail investment products, BETTER FINANCE calls on the ESAs to keep improving their annual costs and performance reports. Currently, the data and coverage of these reports are incomplete and based on commercial databases or surveys. The European Securities Markets Authority (ESMA), the EIOPA and—in the future—the European Banking Authority (EBA) should be able to rely on regular reporting of supervisory data from NCAs, which themselves should have the necessary powers to require regular reporting of data on the costs and performance of saving and investment products in their respective areas of competence.

Going further, the EU legislator should draw inspiration from these examples and incorporate into EU law - specifically, theMiFID and IDD legislation for Pillar III products, currently under review as part of the Retail Investment Strategy (RIS), or the next revision of the IORP II directive on occupational pensions - requirements for NCAs to adequately report figures on a quarterly or monthly basis. This should include the constant updating and public reporting of AuM and net AuM, unit value, asset allocation, as well as the number of participants for all supervised vehicles in the area of long-term and pension savings.

Policy recommendation 2 — Conflicts of interest in scheme management and product distribution

Harmonise and reinforce rules to curb the conflicts of interests in the distribution of long-term and pension saving products, and improve the governance of collective long-term pension schemes.

Conflicts of interest plague the management and distribution of long-term and pension saving products in Europe. The sales commissions-based distribution system of voluntary long-term and pension saving products (Pillar III) directs retail investors towards fee-laden and often underperforming products. Our report showcases various product categories with high average fees and poor long-term returns that so-called "advisors" are paid to recommend to consumers, against the best interest of the latter.

BETTER FINANCE has consistently opposed this system, and strongly supported the European Commission's proposal to partially ban so-called "inducements" as part of the RIS. We believe that the inducements-based distribution system hurts retail investors through higher charges, the illusion of "free" investment advice and a selection bias in distributors' recommendations, all of which result in lower returns and inadequate retirement income for European citizens (BETTER FINANCE, 2023b, pp. 4–13). The financial industry failure to acknowledge the problem and its intense lobbying efforts to maintain a damaging status quo resulted in the utterly disappointing provisional positions of the Council and, especially, the European Parliament (BETTER FINANCE et al., 2024), which should not be expected to improve outcomes for consumers in any meaningful way. Nevertheless, ignoring the problem will hardly make it disappear, and so we urge all involved policy-makers, supervisors, but also willing representatives of the indsutry, to keep working towards the generalisation of high-quality bias-free financial advice that EU citizens can rely for their retail investments.

In occupational pension schemes (Pillar II), the issue of conflicts of interest takes on a different form. In those schemes, it is crucial that the board, which takes decisions on behalf of the scheme's members, includes independent members representing the interests of beneficial owners.

Policy recommendation 3 — Information to (prospective) investors

Provide simple, intelligible, and comparable information on cost and performance of long-term and pension saving products.

Obtaining information on long-term and pension vehicles, as well as monitoring them, should not be difficult for non-professional savers. This implies also reinstating standardised actual cost and past performance disclosure, and in real terms alongside the less relevant nominal ones.

The proposed revisions to the EU's MiFID and IDD legislation, along with the amendments to the PRIIPs regulation, offer the opportunity to finally provide investors with the information they actually need to compare the costs of products. BETTER FINANCE strongly supports, in particular, the provision of annual statements to holders of investment funds' shares distributed under MiFID and to life insurance policyholders distributed under IDD, including the provision of information on the cost of distribution and the possibility to obtain a detailed breakdown of all charges.

Although we welcome the innovations introduced to the format of Key Information Documents (KIDs) by the proposed amendments to the PRIIPs regulation, we still call for a thorough review of this legislation to drastically improve the understandability and comparability of the information provided in the KID. We strongly believe that providers of packaged retail and insurance-based investment products (PRIIPs) should include the actual most recent costs of their products in the KID.

PRIIPs providers should also be required to provide 10 years of past performance data together with the benchmark that is used as investment objective by the product provider. While past performance is not indicative of future performance, it is a good indicator of whether a PRIIP has ever made money or not for the investor, and of an asset manager or insurance company's ability to meet its investment objectives, and to generate returns for the client. Furthermore, it is comparable across product providers and timelines, as it does not rely on assumptions and hypothetical scenarios. The past performance of various products shows how their respective providers navigated through a similar set of real-world circumstances. Finally, displaying past performance in comparison with the product's stated benchmark enables the prospective investor to clearly see whether the provider has been able to make good on their commitment to meet its target.

While we are generally disappointed with the current state of the legislative negotiations on the EU's RIS, we urge the co-legislators to adopt these proposals on disclosures. For more information about our recommendations regarding information to investors and prospective investors, see BETTER FINANCE (2023b, pp. 17–22).

Readers may also refer to BETTER FINANCE's response to the consultation conducted by EIOPA on the review of the Directive on institutions for occupational retirement provision (IORPs) (BETTER FINANCE, 2023a). In occupational pension schemes too, managers should provide pension scheme participants with the information necessary to keep track of their pension benefits and effectively plan their savings and investments to ensure adequate levels of retirement income.

Finally, we urge EU and member state authorities to step up efforts towards the implementation of comprehensive individual pension tracking systems, following the recommendation of the High-Level Forum on the Future of the Capital Markets Union (HLF CMU). These constitute crucial empowering tools, enabling individuals to keep track of their accumulated pension rights across employers and across borders.

Policy recommendation 4 — Sustainability

Provide clear, intelligible information on the sustainability of European long-term and pension savings and investments.

An increasing number of retail investors expresses a desire to invest in financial products that consider sustainability criteria and pursue environmental, social and governance (ESG) objectives (2° Investing Initiative [2DII], 2020). Despite significant progress in recent years, much remains to be done to provide retail investors with an investing environment that accommodates both their financial and sustainability preferences.

First, EU policymakers should increase their efforts to develop a clear, precise, and standardised taxonomy of economic activities. This taxonomy should be grounded in scientific analyses and address all three major aspects of sustainability: environmental, social and governance (ESG). These efforts should also include the development of a well-designed EU-wide Ecolabel for retail investment products that avoids the pitfalls of existing national labels.

EU policy-makers should also address the short-termism of the financial industry by reinforcing the consistent linkage between sustainability and long-term value creation. It must be clearly emphasised that exemplarity with regard to investor protection rules first and ensuring decent returns for individual investors is compatible with investing in a way that respects environment and society. To this end, clear and intelligible ESG disclosures should be combined with financial disclosures, preferably integrated into one document providing savers and investors with a holistic picture of the products they buy.

Finally, EU and national policymakers should require sustainability and ESG knowledge and training for board members in long-term and pension savings vehicles, as well as for financial advisors and sales personnel distributing such products. Regarding the latter, BETTER FINANCE supports the European Parliament's proposal, within the framework of the RIS to impose on financial advisors and sales personnel a yearly training requirement on sustainable investing (see BETTER FINANCE, 2023b, pp. 12–13).

Policy recommendation 5 — Asset allocation

End the fixed-income bias in the asset allocation of long-term savings.

Prudential rules, designed to protect investors against the risk of excessive risk-taking leading to financial losses, require pension fund managers and life insurance providers to allocate a significant portion of participants' and policyholders' funds into fixed-income assets, particularly sovereign debt from EU Member States.

However, in doing so, these rules excessively restrict the possibility for long-term and pension savers to take advantage of investment opportunities in equity markets, which, while more volatile, also offer higher yields in the long term.

Regulations governing long-term and pension savings should not discriminate against long-term equity investments. Specifically, life-cycling strategies that adjust risk to the investment horizon of the saver should enable managers to invest a substantial portion of younger investors' contributions or premiums in equity market instruments (as is the case of Sweden's Premium pensions, in particular the AP7 Såfa fund).

Policy recommendation 6 — Taxation

Stop penalising taxation of long-term and pension products.

Taxation on pensions, whether on contributions, returns, or payouts, should be based on real values rather than nominal ones. Taxes should be applied to values adjusted for inflation, using the harmonised index of consumer prices (HICP). To recoup the value of pension pots, at least occupational schemes (Pillar II) should apply an "EEE" regime. Pillar II contributions should be deductible from the income base tax.

Policy recommendation 7 — Pan-European Pension Product (PEPP)

Create a friendly environment for the PEPP

This year's report, for the first time, includes cost and performance data on PEPP, as implemented in Slovakia. As previously mentioned, these data are encouraging. Nevertheless, we note that the current environment is not conducive to the take up of this product, despite its intrinsic qualities from the point of view of retail investors:

- As noted by EIOPA:

  > [t]he higher costs of products considered "competitors" to PEPP may diminish its appeal to potential providers. [...] Offering a cheaper enquotecompetitor product might raise concerns about the risk of product cannibalisation, potentially resulting in a loss of sales and revenue from existing products4 (EIOPA, 2024).

  Shielded from competition by the opacity of costs and performance disclosures, and the dominant inducements-based distribution system that biases "enquote" towards high-fee products, incumbent providers have little incentives to add a low-cost product to their range of personal pension products.

- Member State governments have generally failed to ensure that PEPP competes on a level playing field with existing personal pension products: rules on tax rebates and subsidies applicable to equivalent personal pension products have only in a few cases been extended to the PEPP, and transferability of accrued personal pension benefits from existing products to PEPP is only possible in a handful of Member States (EIOPA Occupational Pensions Stakeholder Group [OPSG], 2024).

BETTER FINANCE urges policy-makers not to give in to industry pressures to delete the 1% fee cap for the Basic PEPP. Instead,

- Member States should amend their respective legislations to ensure that PEPP receives the same treatment as any other personal pension product marketed in their jurisdiction.
- EU and Member State authorities must further explore the suggestions put forward by EIOPA in its recent paper to expand the target market for PEPP with a view to offer potential PEPP providers the perspective of greater economies of scale.

Policy recommendation 8 — Auto-enrolment

Introduce auto-enrolment in occupational pensions.

The active labour force should be automatically enrolled in a default pension fund, with the option to withdraw or switch provider at no additional cost. Romania, Sweden, Slovakia and other serve as best practice examples: This auto-enrolment ensures that working individuals start saving early and consistently for their retirement, reducing the risk of insufficient income in retirement. This was also a recommendation of the HLF CMU.

In this regard, we consider with interest EIOPA's suggestion, in its paper from September 11, 2024 to enable the use of PEPP as an occupational pension product, in which employers could then automatically enrol their workforce (EIOPA, 2024).

Policy recommendation 9 — Suspensions

Allow savers to defer contributions to pensions without penalties.

Savers should be allowed to suspend payments into a pension savings or life insurance plan without incurring a penalty. In an era characterised by uncertainty, it can never be assumed that an individual will always have an income sufficient to cover their immediate needs as well as pay their premium or set contribution towards their pension plan.

When an individual, for whatever reason, cannot, for a short period of time, contribute to their pension product, they should not be faced with the choice between foregoing their pension plan or paying a penalty. Instead, they should be able to suspend payments and resume as soon as they have a new income stream.

Policy recommendation 10 — Insurance guarantee schemes

Urgently establish harmonised insurance guarantee schemes in the EU.

EU citizens are partially covered against the default of product manufacturers through

Directive 2014/49/EU on deposit guarantee schemes (DGSs) and Directive 97/9/EC on investor compensation schemes (ICSs). However, many pension savers across the EU lack an appropriate protection for insurance-based investment products (IBIPs), a shortcoming of the EU's protection regime that is particularly problematic as IBIPs (such as life insurance) are predominant in some pensions systems in the EU (e.g., in France).

BETTER FINANCE calls on the EU legislator to revamp the project for a Regulation on insurance guarantee schemes (IGSs), which should mimic the rules of the DGS Directive, and urgently harmonise protection against defaults at a minimum level across the EU.

References

2° Investing Initiative. (2020, March). *A large majority of retail clients want to invest sustainably. Survey of French and German retail investors' sustainability objectives*. Retrieved September 14, 2023, from https://2degrees-investing.org/wp-content/uploads/2020/03/A-Large-Majority-of-Retail-Clients-Want-to-Invest-Sustainably-Final.pdf

BETTER FINANCE. (2023a, May 26). *BETTER FINANCE response to EIOPA consultation on technical advice on IORP II review* (Response to consultation). Brussels. Retrieved February 29, 2024, from https://betterfinance.eu/publication/better-finance-response-to-eiopa-consultation-on-technical-advice-on-iorp-ii-review/

BETTER FINANCE. (2023b, October 19). *BETTER FINANCE's key position on the Retail Investment Strategy proposals* (Position paper). Brussels. Retrieved February 14, 2024, from https://betterfinance.eu/publication/better-finance-position-on-the-retail-investment-strategy/

BETTER FINANCE, BEUC, & Finance Watch. (2024, March 18). *Retail Investment Strategy: A "compromise" that undermines the Capital Markets Union and harms retail investors* (Joint statement). Brussels. Retrieved April 5, 2024, from https://betterfinance.eu/publication/joint-consumer-organisations-statement-on-the-retail-investment-strategy-compromise-proposal/

EIOPA Occupational Pensions Stakeholder Group. (2024, July 31). *Pan-European Pension Product: Market development, Challenges, Obstacles, Solution* (Own-initiative OPSG Discussion Paper No. OPSG-24/21). European Insurance and Occupational Pensions Authority. Frankfurt-am-Main. Retrieved September 19, 2024, from https://www.eiopa.europa.eu/document/download/88c75466-65ac-422c-a0bd-0c0b178db8fb_en?filename=OPSG-2024-21%20OPSG_Own-initiative%20Discussion%20Paper%20on%20Pan-European%20Pension%20Product%20-%20Market%20development%2C%20Challenges%2C%20Obstacles%2C%20Solutions.pdf

European Insurance and Occupational Pensions Authority. (2020, August 14). *Pan-European Personal Pension Product (PEPP): EIOPA's stochastic model for a holistic assessment of the risk profile and potential performance* (EIOPA-20-505). Frankfurt-am-Main. Retrieved November 23, 2023, from https://www.eiopa.

europa.eu/system/files/2020-08/eiopa-20-505_pepp_stochastic_model.pdf

European Insurance and Occupational Pensions Authority. (2024, September 11). *A simple and long-term European savings product: The future Pan-European Pension Product* (EIOPA staff paper). Frankfurt-am-Main. Retrieved September 11, 2024, from https://www.eiopa.europa.eu/document/download/53a75b6e-fc6b-46ce-9818-02badf20f515_en?filename=EIOPA%20Staff%20Paper%20on%20the%20future%20Pan-European%20Pension%20Product.pdf

McGuinness, M. (2023, April 27). *Speech by Commissioner McGuiness at Eurofi High-Level Seminar* (Speech). Stockholm. Retrieved January 15, 2024, from https://ec.europa.eu/commission/presscorner/detail/en/speech_23_2492

Country Case 12

Romania

Rezumat

Populația României scade rapid, îmbătrânește și migrează, ceea ce pune o presiune considerabilă asupra sistemului public de pensii. În 2019, au fost adoptate noi modificări privind calcularea pensiilor pentru limită de vârstă din pilonul de plată, în vigoare din septembrie 2021 și modificate în continuare în 2023 pentru a aduce mai multă stabilitate fiscală sistemului de pensii.

Deși pensiile ocupaționale sunt obligatorii indiferent de forma de muncă (salariați și liber-profesioniști), gospodăriile din România trebuie să fie mai mult stimulate să economisească în planuri de pensii facultative (Pilonul III). Planurile de pensii private din România au înregistrat un randament nominal pozitiv excepțional în 2023. În medie, randamentele nominale pentru 2023 au fost de 17,2% pentru fondurile din Pilonul II și de 17,8% pentru fondurile din Pilonul III. Cu toate acestea, inflația încă ridicată a redus randamentele la jumătate în 2023.

Ambele sisteme (ocupațional și privat) au structuri de portofoliu aproape identice și generează astfel randamente brute similare. Cu toate acestea, performanța netă a Pilonului III este influențată în mod semnificativ de structura comisioanelor ridicate (de aproape 4 ori mai mari în comparație cu fondurile Pilonului II) și, pe termen lung, va genera randamente mai mici decât cele ale fondurilor similare Pilonului II. În general, randamentul real al fondurilor de pensii din Pilonul II este încă ușor pozitiv pentru întreaga istorie, cu toate acestea, fondurile din Pilonul III rămân în teritoriu negativ pentru întreaga istorie, chiar și după randamentele solide din 2023.

Summary

Romania's population is rapidly decreasing, ageing, and migrating, which puts considerable pressure on the State pension system. In 2019, new changes on calculating old-age pensions from pay-as-you-go (PAYG) pillar have been adopted effective since September 2021 and further amended in 2023 to bring more fiscal stability to the pension system.

Although occupational pensions are mandatory regardless of the work form (employees and self-employed), the Romanian households must be incentivised more to save in voluntary pension plans (Pillar III). Private pension schemes in Romania recorded an exceptional positive nominal returns in 2023. On average, nominal returns for 2023 were 17.2% for Pillar II funds and 17.8% for Pillar III funds. However, the still elevated inflation cut the returns by half in 2023.

Both schemes (occupational and private) have almost identical portfolio structures and thus generate similar gross returns. However, Pillar III net performance is significantly influenced by the high fee structure (almost 4-times higher compared to Pillar II funds) and will, in the long-run, deliver lower returns than Pillar II peers. Overall, the real return of pension funds in Pillar II are still mildly positive for the entire history, however, Pillar III funds stay in the negative territory for the entire history even after solid returns in 2023.

Introduction: The Romanian pension system

- Private pension schemes in Romania recorded an exceptional positive nominal performance in 2023. On average, nominal returns for 2023 were 17.22% for Pillar II funds and 17.77% for Pillar III funds. It should be noted, that the portfolio structure of almost all pension funds in Pillar II and Pillar III is similar and the savers are of limited choice regarding the investment strategy.

- Real returns of all funds in both pillar were significantly affected by elevated inflation in 2023. Real returns for both pillars were cut by the inflation to 9.34% for mandatory pension funds (Pillar II) and 8.27% for voluntary pension funds (Pillar III) in 2023.

Table RO.1 – Long-term and pension savings vehicles analysed in Romania

Product	Pillar	Reporting period *Earliest data*	*Latest data*
Mandatory pension funds	Occupational (II)	2008	2023
Voluntary pension funds	Voluntary (III)	2007	2023

Table RO.2 – Annualised real net returns of Romanian long-term and pension savings vehicles (before tax, % of AuM)

	Mandatory pension funds	Voluntary pension funds
1 year (2023)	9.3%	8.3%
3 years (2021–2023)	-3.4%	-4.5%
5 years (2019–2023)	-0.7%	-1.8%
7 years (2017–2023)	-0.9%	-2.0%
10 years (2014–2023)	0.8%	-0.3%
Whole period	1.3%	-1.4%

Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE.

- Romania has committed to reforming the first pillar of its pension system under the recovery plan financed by the EU by the end of 2023.

- The reforming plans include gradual increase of the retirement age to 65 years (a move pertaining to the public pension system, but also the employees subject to special pensions) and calculating the pension based on the entire working period and not allowing pension benefits highest than the net wages received by same recipients.

- The reform should by focused on fair treatment of so-called special service pensions. These are pensions granted to certain professional categories such as judges, prosecutors, military, police and secret service employees, some of which are even ten times higher than the average pension in the country. These special pensions are still not based on the contributory principle and are considered a burden on the state budget.

Pension system in Romania: An overview

The Romanian old-age pension system is based on the World Bank's multi-pillar model, which consists of three main pillars:

- Pillar I — State pension organized as a mandatory PAYG scheme;
- Pillar II — Organised as a mandatory, funded and hybrid defined contribution (DC) pension scheme,
- Pillar III — A supplementary pension scheme, based on the principle of voluntary participation with hybrid DC characteristics.

Romania's multi-pillar pension reform began in 2007, when Pillar III was added into the pension system (collecting the first contributions) and became voluntary for all persons earning any type of income. Pillar II was put into place in 2008 (collecting the first contributions) and became mandatory for all employees aged under 35.

Table RO.3 and text provide an overview of the Romania's pension system. It contains information on main characteristics of each pillar, main pension savings vehicles, respective coverage of each pillar.

The overall coverage of Pillar II was almost entire working population, while Pillar III covered only 10% of the economically active population. Thus, we can expect than future pension income stream will be influenced mostly by Pillar II pensions, while Pillar III will generate an insignificant part of individuals income during retirement.

The first pillar of the Romanian pension system is organized on the PAYG principle of redistribution, being funded on an ongoing basis and functioning on the defined-benefit rule.

The state (through the National House of Public Pensions, a public institution constituted for this purpose in particular) collects the social pension contribution from the contributors and immediately pays the pensions to the current retirees. State pension in Romania is also based on the principle of solidarity between generations and gives the right to pension entitlement upon retirement age, following a minimum contribution period (15 years), as provided by law. This compulsory system is closely connected to the economic activity and income of citizens. It is 88% financed from social security contributions made by both employers and by employees, while generally consuming the biggest part (or entirety) of the social security budget.

According to Romania's legislation until 2023, the standard retirement age is 63 years for women and 65 years for men. These levels were to be gradually reached as follow:

Table RO.3 – Overview of the Romanian pension system

Pillar I	Pillar II	Pillar III
State Pension	Funded pension	Voluntary pension
Law no. 263/2010 on the unitary public pension system	Law no. 411/2004 on the privately managed pension funds, republished, including subsequent amendments and additions	Law no.204/2006 on the voluntary pensions, including subsequent amendments and additions
Mandatory	Mandatory	Voluntary
Publicly managed	Privately managed pension funds	
PAYG	Funded	
Defined benefit (DB) scheme	DC schemes Individual personal pension accounts	
The possibility of early and partially early retirement, contingent upon the fulfillment of the age conditions and the contribution stage provided by the law and the accumulated points.	Withdrawal from the system is only allowed through retirement at standard retirement age.	The participant can, at any time, suspend or stop the contribution payment (they remain members in the system until 60 years old).
Quick facts		
Nb. of old-age pensioners: 4.61 mln.	Administrators: 7	Administrators: 8
Nb. of insured: 6.31 mln.	Funds: 7	Funds: 10
Avg. old-age pension: EUR 425	Custodians: 3	Custodians: 3
Average salary (gross): EUR1 668	Brokers: 14	Brokers: 21
Gross replacement ratio (state pension): 25.46%	AuM EUR 25.46 bln.	AuM: EUR 0.96 bln.
	Participants: 8.168 mln.	Participants: 0.77 mln.

Data: CNPP, ASF and INSSE, 2024;
Note: data on average old-age pension and gross salary and data on the number of old-age pensioner are as of December 2023; data on number of participants and assets under management as of December 2023.

- between January 2011 and January 2015, the standard age for the pensioning of women will grow from 59 years to 60 years and for men from 62 years to 65 years;
- at the end of 2015 period retirement age will gradually increase only for women from 60 years to 63 years until 2030.

Early retirement: According to Law no. 263/2010 regarding the public pension schemes (in force since 1 January 2011) claiming early pension is possible as of a maximum 5 years before the standard retirement age, provided the worker has at least eight or more contribution years. The deduction made on early pension payment is fixed at 0.75% for each month (9% per year), which might bring a maximum deduction of 45% from the standard pension. The deduction is applied until the standard age limit is reached.

Year 2023 introduced new legislature (No. 360/2023) that was part of the Recovery plan pension reform. The new legislation:

- introduces a new calculation formula for new pensions and pensions in payment. The parameters of the formula shall be carefully chosen in line with the target for pension expenditure as percentage of GDP. Moreover, they shall not allow for ad hoc increases on pension levels;
- introduces a new pension indexation rule in line with the pension expenditure as percentage of GDP target and mechanisms against ad hoc indexation;
- significantly reduces possibilities for early retirement, introduce incentives to expand the working life and to voluntary increase standard retirement age up to 70 years in line with the increases of life expectancy, and equalize the statutory retirement age for men and women at 65 years by 2035;
- starts gradually lift the retirement age also for woman to 65. However, the new law introduces the deduction from the statutory retirement age based on the number of raised children, more specifically 6 months per child; introduces incentives for postponing retirement;
- revises special pensions to bring them in line with the contributory principle;
- strengthen the contributory principle of the system;
- increases the adequacy of minimum and lower pensions, in particular for those below the poverty threshold.

Furthermore, the financial viability of the Pillar II of the pension system was ensured by increasing contributions to this pension pillar.

Romania's mandatory private pensions system (Pillar II) is a fully funded scheme, with mandatory participation and private management of funds based on personal accounts and on the DC philosophy with minimum return guarantees. The minimum return guarantee means that participants will receive at least the sum of contributions, net of fees, at retirement. Each fund has to comply, during the accumulation phase, with a minimum return mechanism that is set quarterly by national regulation and based on average market performance of all funds. Pillar II represents the privately managed mandatory pensions funds or schemes.

Pillar II has been mandatory since its inception for all employees paying social security contributions under the age of 35 and voluntary (optional) for employees aged 35 to 45.

Contribution collection is centralized by the *Casa Națională de Pensii Publice* (CNPP), the Romanian national house of public pensions, which collects and directs the contributions towards the mandatory pension funds.

A participant contributes during his active life and will get a pension when reaching the retirement age. The starting level of contribution was at 2% of the participant's total gross salary and it should go up by 0.5 percentage points a year, to reach 6% of total gross revenues in 2017. However, these values were never reached and the value for 2019 3.75 p.p. The contribution level is fixed, with no possibility to contribute less or more based on individual preferences.

The contributions to a pension fund are recorded in individual personal pension account. The savings are invested by the pension fund administrator, according to the rules and quantitative limits generally set by the law regulating Pillar II vehicles. Participants can choose only one pension fund. Withdrawal from the Pillar II is only allowed at the standard retirement age of participants in the private pension system.

Mandatory pension funds are managed by their administrators, Pension Management Companies (PMCs). Each PMC can manage only one mandatory pension fund. Mandatory pension funds operations are similar to the investment funds. PMCs must obtain several licenses from Romania's pension market regulatory and supervisory body, which is the *Autoritatea de Supraveghere Financiară* (ASF), the Financial Supervisory Authority.

The ASF is in charge of control, regulation, supervision and information about private pensions as an independent administrative authority and legal entity under the control of the Romanian Parliament.

Romania's voluntary private pensions system Pillar III is also based on the World Bank's multi-pillar model. It is also a fully funded system, based on personal accounts and on the DC philosophy. Pillar III represents privately managed supplementary, voluntary pensions.

In Pillar III, participation is open to everybody earning an income, either employees or the self-employed. Contributions are generally made through the employers in case of employees. In case of self-employed, the contributions are sent directly on the accounts managed by pension management companies. The contributions are made by the employee, with the possibility for employers to contribute a share.

Pillar III is fully voluntary and the contributions are invested via voluntary pension funds as a special purpose vehicle that are managed by their administrators - PMCs, Life Insurance Companies (LICs) or Asset Management Companies (AMCs). Each administrator is obliged to establish and operate at least one voluntary pension fund. However, in contrast to Pillar II, administrators can manage as many funds as they wish. A voluntary pension fund operates on a similar basis as investment fund. Pension fund administrators must get several licenses from Romania's ASF.

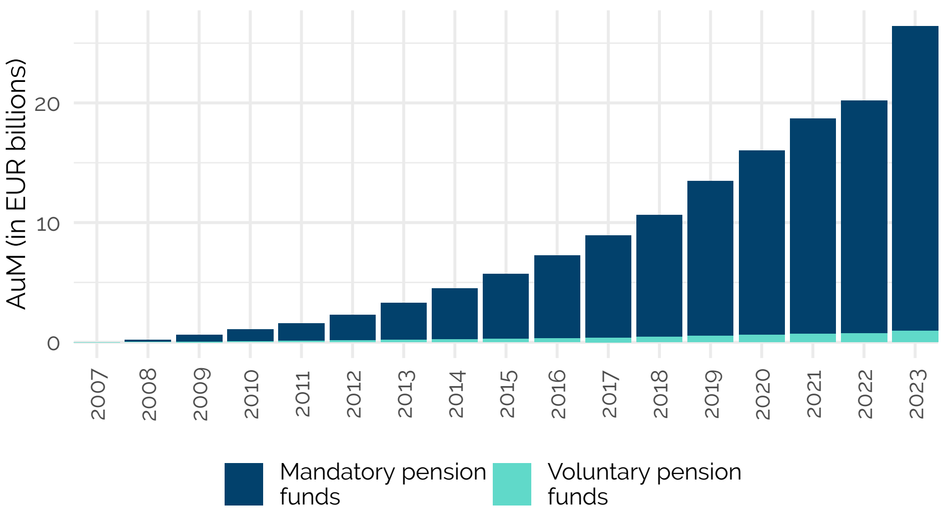
Participants to a voluntary pension fund contribute during their active life and will get a pension at the age of 60 (both woman and men) if he had accumulated at least 90 contributions. The contribution is limited up to 15% of the participant's total gross income. The contribution level is flexible: it can be decided upon, changed, and even interrupted and resumed.

Long-term and pension savings vehicles in Romania

Pension saving vehicle for both pillars in Romania are based on a saving principle with investment strategies and realized via pension funds. The transparency of information regarding the pension funds is really high in Romania, where all key information on performance, fees, risk and portfolio structure are well presented to the public.

AuM for pension funds offered under both pillars (in million EUR) are presented in Figure RO.1. Pillar II plays dominant role and represents more than 97% of pension savings in Romania.

Figure RO.1 – AuM of Romanian long-term and pension savings vehicles



Data: CSSPP; *Calculations:* BETTER FINANCE.

In Pillar II, seven asset managers offer seven mandatory pension funds in Romania. Performance analysis reveals similarities in their investment strategy, implying similarity in the pension funds' portfolio structure.

In Pillar III, eight asset managers offer 10 voluntary pension funds in Romania. AZT and NN are the only providers which offer two voluntary pension funds. The performance of all pension funds shows the same finding as for the Pillar II mandatory pension funds—there is similarity in voluntary pension funds' investment strategy. Performance results also imply a similarity in pension funds' portfolio structure.

Second pillar: Mandatory pension funds

As indicated above, each PMC specifically authorized to provide Pillar II savings products in Romania is allowed to manage only one mandatory pension fund. At the introduction of the Pillar II, the total number of authorized administrators (funds) was 18. Consolidation started as early as 2009 and 2010.

Currently (end of 2023), there are 7 administrators offering 7 pension funds. The two biggest mandatory pension funds (AZT and NN) dominant the market with cumulative market share above 50%.

Each PMC is authorized and supervised by ASF. One of the most important conditions imposed on PMCs is to attract at least 50000 participants. ASF withdraws the fund's authorization if the number of participants drops below 50000 for a quarter.

Mandatory pension funds' investment strategy is very strictly regulated. The law imposes percentage limits for different asset classes. Mandatory pension funds can invest:

- up to 20% in money market instruments;
- up to 100% in State bonds of Romania, the EU or European Economic Area (EEA);
- up to 30% in bonds and other transferable securities issued by the local public administrations in Romania, the EU or EEA, traded on a regulated market in RO, EU or EEA;
- up to 50% in securities traded on a regulated market in Romania. the EU or EEA;
- up to 15% in bonds issued by third-party states, traded on a regulated market in Romania, the EU or EEA;
- up to 10% in bonds and other transferable securities issued by the local public administration in third-party states, traded on a regulated market in Romania. the EU or EEA;
- up to 15% in bonds issued by the World Bank. the European Bank for Reconstruction and Development and the European Investment Bank, traded on a regulated market in Romania, the EU or EEA;
- up to 5% in bonds issued by Non-governmental Foreign Bodies, traded on a regulated market in Romania, the EU or EEA;
- up to 5% in units issued by undertakings for collective investment in transfer-

able securities (UCITSs), including exchange-traded funds (ETFs) in Romania, the EU or EEA;

- up to 3% in ETCs and equity securities issued by non UCITSs set up as closed investment funds, traded on a regulated market in Romania, the EU or EEA;
- up to 10% in private equity—only for voluntary pension funds.

There is no explicitly defined general quantitative limit on equity investments.

Aside from the quantitative restrictions by asset class, fund managers have quantitative limits by type of issuer:

- 10% of the total number of shares issued by one issuer;
- 10% of the preferential shares issued by one issuer;
- 25% of the equity securities issued by an UCITS, ETF, non-UCITS closed investment fund or ETC;
- 10% of an issuer's bonds, with the exception of the state bonds.

Mandatory pension funds can invest all their assets abroad. There are no explicit restrictions regarding investments made abroad.

Pension funds can have one of three possible risk profiles, which are calculated on a daily basis according to a formula established by ASF regulations:

1. low risk (risk level up to and including 10%),
2. medium risk (risk level between 10%, exclusively, and 25%, inclusively),
3. high risk (risk level between 25%, exclusively, and 50%, inclusively).

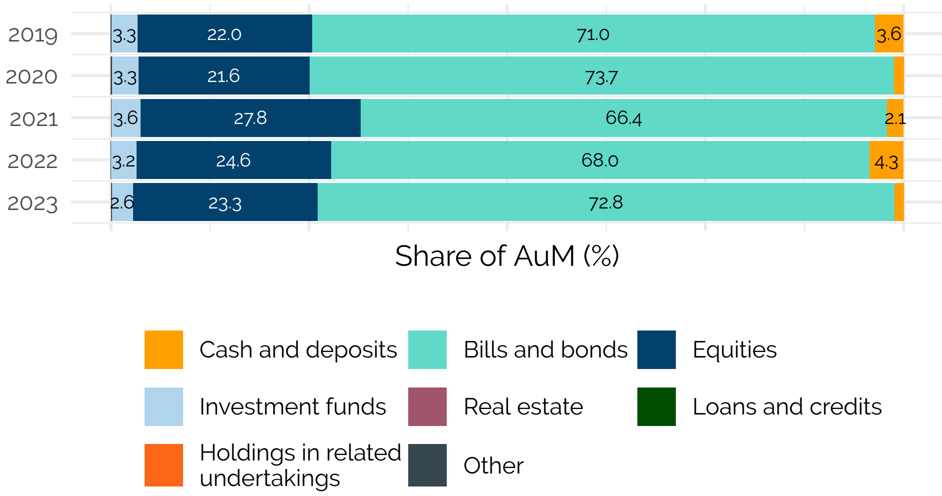
Pillar II mandatory pension funds portfolio structure is presented in Figure RO.2.

Romanian mandatory pension funds invest mostly in government securities and bonds asset classes. The second most important asset class (from the portfolio structure point of view) are equities and the third most important are bank deposits. Three other classes have minimal impact on pension fund's performance. The portfolio structure of the Romanian Pillar II is presented below. According to the data available, currently almost 73% of all investments in Pillar II pension funds are bond investments and less than 23% is invested in equities despite relatively young age structure of savers.

Third pillar: Voluntary pension funds

The Romanian Pillar III allows each administrator (PMC, LIC or AMC) to manage as many voluntary pension funds as they prefer. At its inception, there were only four providers and six voluntary pension funds. Currently (at the end of 2021), there was 8 providers offering 10 voluntary pension funds. Only two administrators (NN and AZT) are currently offering more than one voluntary pension fund.

Figure RO.2 – Allocation of Romanian mandatory pension funds' assets



Data: ASF Romania; *Calculations:* BETTER FINANCE.

Each administrator in Pillar III (PMC, LIC or AMC) is authorized by ASF and must get several licenses from ASF. ASF withdraws the fund's authorization if the number of participants drops below 100 for a quarter.

Voluntary pension funds are also constituted by civil contract and authorized by ASF. Accounting of the voluntary pension fund is separated from the administrator.

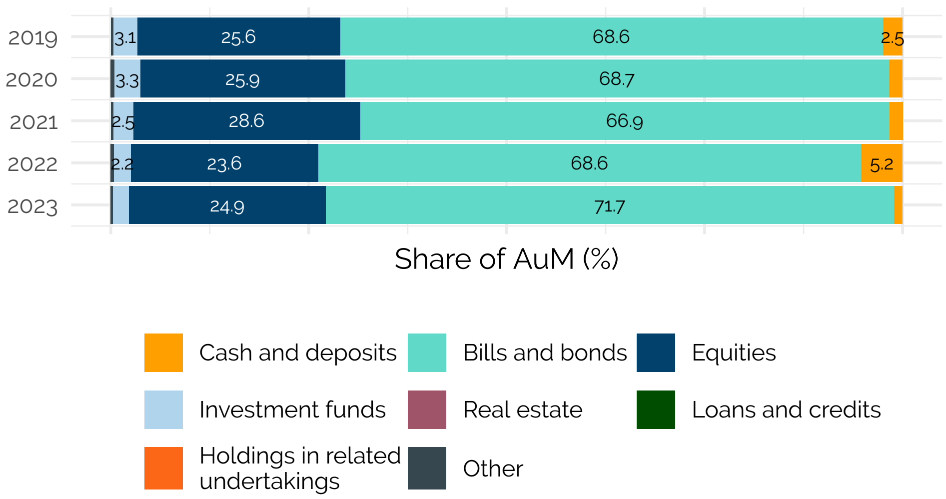
Investment rules in the voluntary private pension pillar are the same as in the mandatory pillar (see quantitative and restriction limits for different asset classes in the text above), with less strict limits on private equity (5%) and commodities (5%).

Analysing the portfolio structure of voluntary pension funds based on *Comisia de Supraveghere a Sistemului de Pensii Private* (CSSPP) data, we can conclude that most of the performance is tied to the Government Securities and Bonds asset classes. The second most important asset class (from the portfolio structure point of view) are the equities and the third most important part of the portfolio are the bank deposits. Other asset classes have minimal impact on pension fund's performance results.

Portfolio structure of Romanian Pillar III voluntary pension funds is presented in Figure RO.3.

According to the data for 2023, around 72% of all investments in Pillar III pension funds are bond investments and about 25% is invested in stocks and collective investment vehicles (UCITSs funds). Overall, Pillar III portfolio structure is very similar to that of Pillar II over the whole analysed period. The difference in the performance could therefore be devoted to the negative impact of fees, which are significantly higher in Pillar III.

Figure RO.3 – Allocation of Romanian voluntary pension funds' assets



Data: ASF Romania; *Calculations:* BETTER FINANCE.

Charges

Charges in both pillars are regulated differently. As the Pillar II is more regulated and represents the dominant role for the future pension income stream, the regulation of fees and charges pushes the overall costs down for Pillar II pension funds compared to the Pillar III peers.

Charges of Pillar II products: Mandatory pension funds

According to the Mandatory Pensions Law, the fund manager's income resulted from the administration of privately administrated pension funds are composed of:

1. Entry fee used to reach up to 1% of the contributions paid (entry fee was paid before the conversion of contributions into fund units, of which 0.5% was transferred to the CNPP, the organization that administers the social insurance program), but no entry fee are levied any more since December 2022;

2. Management fee — from 0.02% to 0.07% monthly of net assets under management, depending on the fund's rate of return relative to the inflation rate. Before 2019, the maximum monthly management fee was 0.05 percent.

3. Transfer penalties (covered from personal assets, in case of moving to another fund/PFC earlier than in 2 years — up to 5%);

The transfer penalty represents the amount paid by the participant in the event of a transfer to another administrator, occurring within two years of the subscription date to the private pension fund, with the maximum ceiling of this penalty being established by ASF and set at maximum 5% of assets (Norm CSSPP 12/2009 for

Pillar II and Norm 14/2006 for Pillar III).

The fund also pays for the annual auditing fee (Fund auditing taxes) and the rest of the fund's expenses (custody, depositary, transaction/trading expenses) must be supported by the pension company (the administrator). The next table compares effective charges of mandatory pension funds in Pillar II over time, calculated via total and net asset value (NAV).

The year 2023 brought further decrease in fees for pension administrators in Pillar II, while the effective charges dropped down to 0.22% annually.

Table RO.4 presents the effective annual charges for mandatory pension funds (in percentage of NAV).

Table RO.4 – Costs and charges of Romanian mandatory pension funds (% of assets)

Year	Total ongoing charges
2008	0.77%
2009	0.70%
2010	0.66%
2011	0.61%
2012	0.62%
2013	0.61%
2014	0.60%
2015	0.60%
2016	0.58%
2017	0.56%
2018	0.61%
2019	0.51%
2020	0.51%
2021	0.48%
2022	0.24%
2023	0.22%

Data: ASF Romania; *Calculations:* BF; *Note:* Data as of December 2023.

Charges of Pillar III producs: Voluntary pension funds

According to the Voluntary Pensions Law, the administrator shall charge a fee from participants and beneficiaries for the management of a pension fund.

- The levels of fees shall be established in the pension scheme prospectus and shall be the same for all participants and beneficiaries;
- Participants shall be notified of any change to the fees at least 6 months before it is applied.

The administrator's revenue will come from:

- management fee — charged as a percentage from the net assets of the voluntary pension fund; this percentage cannot be higher than 0.2% per month and shall be mentioned in the pension scheme prospectus;
- transfer penalties (covered from personal assets, in case of moving to another fund/PFC earlier than in 2 years — 5%);

A transfer penalty is applicable (paid by the participant) in the event of a transfer to another fund within two years of having joined the previous fund; its upper limit is established by Commission norms. Table RO.5 compares effective charges of voluntary pension funds in pillar III over time (calculated via total and net NAV).

Table RO.5 – Costs and charges of Romanian voluntary pension funds (% of assets)

Year	Total ongoing charges
2007	4.72%
2008	1.91%
2009	2.12%
2010	2.30%
2011	2.09%
2012	2.10%
2013	1.99%
2014	1.99%
2015	2.01%
2016	1.92%
2017	1.83%
2018	1.99%
2019	1.99%
2020	1.98%
2021	1.96%
2022	1.94%
2023	1.84%

Data: ASF Romania; *Calculations:* BF; *Note:* Data as of December 2023.

The analysis confirms that despite the almost same portfolio structure and same performance, Pillar III pension funds are almost seven times more expensive than Pillar II funds, charging almost 1.84% annually in 2023. The decrease in Pillar III charges is recorded in 2023, but only on a small scale.

Taxation

Romania applies an EET system for the taxation of future mandatory accounts. Employee contributions are tax-deductible and investment income on the level of the pension fund is tax-exempt. Pension benefits paid out during retirement will be subject to a personal income tax (10% tax rate) above a certain level.

The amount of contributions to voluntary pension funds is fiscally deductible from each subscriber's gross monthly wage or any other assimilated revenue if the total amount is not greater than the equivalent in Romanian Leu (RON) of EUR 400 in a fiscal year. The same rule applies to the employer, meaning that the employer can deduct the amount paid to the employee's voluntary pension account up to EUR 400 annually. The investment returns achieved by the third pillar fund are tax exempt until the moment of payments toward subscribers' start. The pension benefits paid from Pillar III are subject to personal income tax, thus representing an "EET" regime.

Table RO.6 – Taxation of pension savings in Romania

Product	Phase			Regime
	Contributions	*Investment returns*	*Payouts*	
Mandatory pension funds	Exempted	Exempted	Taxed	EET
Voluntary pension funds	Exempted	Exempted	Taxed	EET

Source: Own elaboration.

Performance of Romanian long-term and pension savings

Real net returns of Romanian long-term and pension savings

Romania is a high inflation country. The average annual inflation rate between years 2001 and 2023 was 9.28%, while for the rest of the EU, the annual inflation rate was 6.38%. Thus, we can expect that the inflation will have a significant effect on the real returns of pension vehicles.

Figure RO.4 shows two charts presenting the development of the inflation in Romania.

The performance of pension funds for both pillars in Romania are presented in Figures RO.5 and RO.6.

When inspecting the development of the performance of pension products within each pillar, the inflation do play a key role in maintaining the buying power of the savings for the retirement age.

For pillar III voluntary pension funds performance, the fees and charges are the second factor influencing the real value of savings.

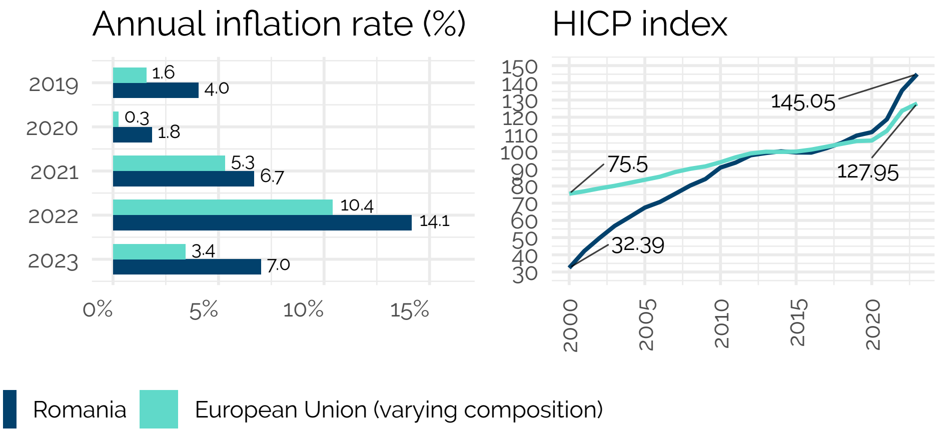
Figures RO.7 and RO.8 show the nominal and real net performance of pension funds for both pillars.

For voluntary pension funds, the fees and charges decrease the performance of funds by almost half, indicating more room for cost-effectiveness.

Figure RO.4 – Inflation in Romania

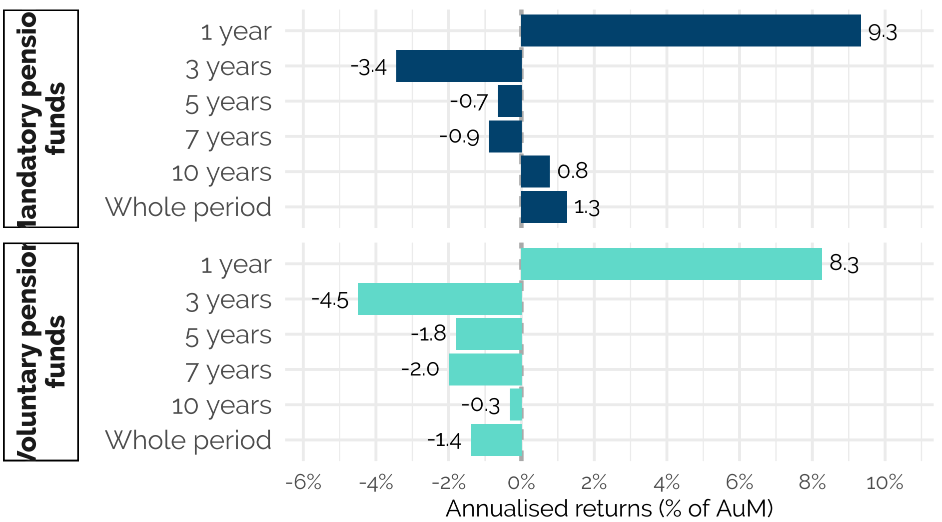
Period 2000–2023

	Annualised	Cumulated
Romania	8.0%	530.1%
European Union (varying composition)	2.3%	73.2%



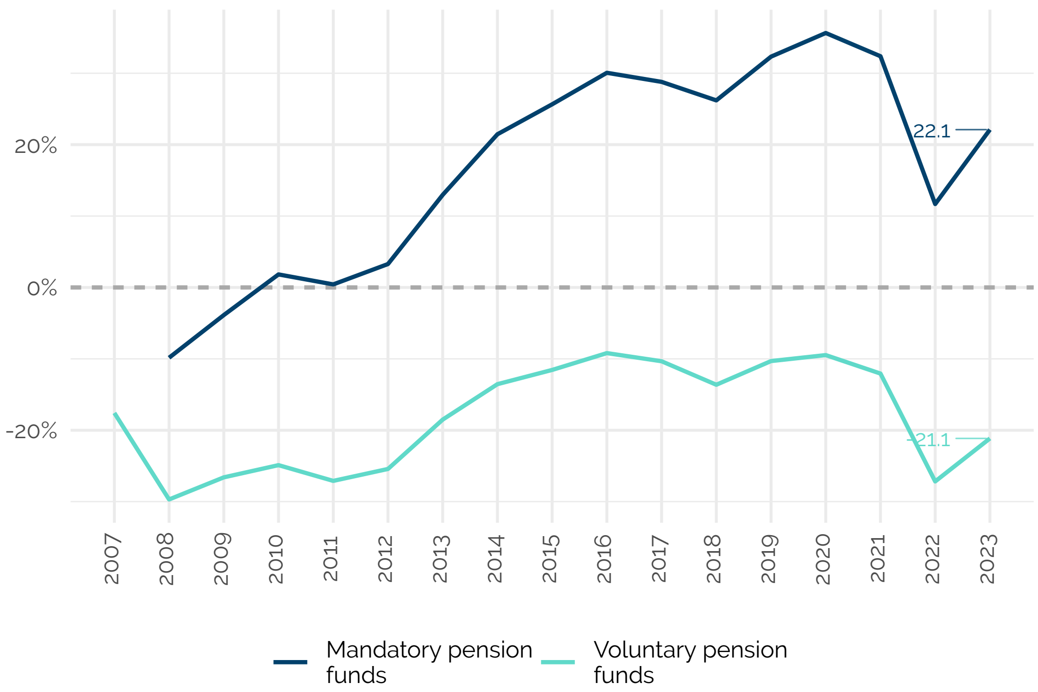
Data: Eurostat, HICP monthly index (2015 = 100); *Calculations:* BETTER FINANCE

Figure RO.5 – Annualised returns of Romanian long-term and pension vehicles over varying holding periods (before tax, % of AuM)



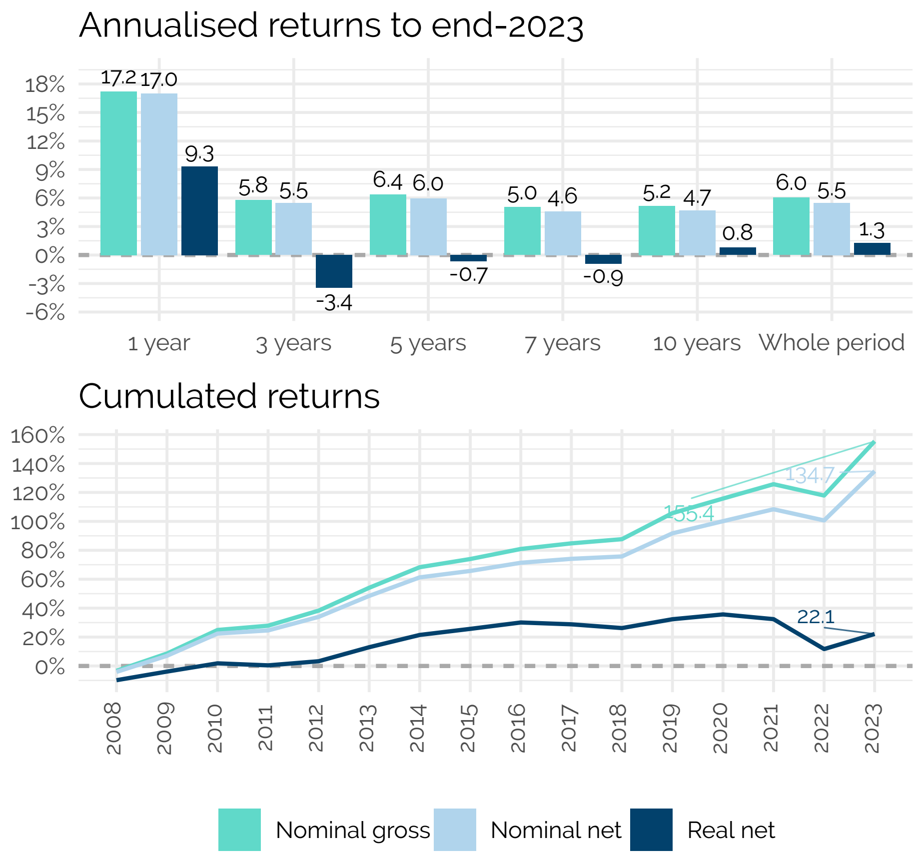
Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE, holding periods to end-20

Figure RO.6 – **Cumulated returns of Romanian long-term and pension savings vehicles (2003–2023, before tax, % of AuM)**



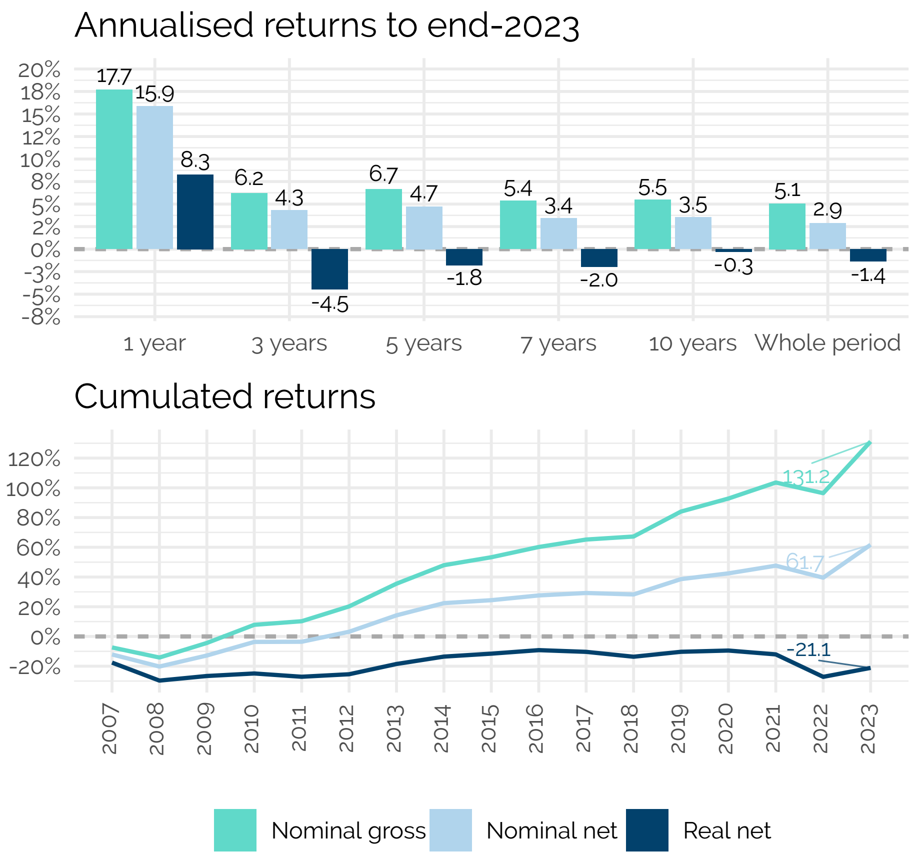
Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE.

Figure RO.7 – Returns of Romanian mandatory pension funds (before tax, % of AuM)



Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE, holding periods to end-2

Figure RO.8 – Returns of Romanian voluntary pension funds (before tax, % of AuM)



Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE, holding periods to end-2

Do Romanian savings products beat capital markets?

In this section, we compare the performance of the Romanian Pillar II and Pillar III pension funds to the performance of relevant capital market benchmarks. In order to do so, we have analysed the portfolio structure of pension funds and set the weight of asset classes for the benchmark portfolio creation.

We have set the weight of the equities at 20% of the benchmark portfolio.

Table RO.7 – Capital market benchmarks to assess the performance of Romanian pension vehicles

Product	Equity index	Bonds index	Allocation
Mandatory pension funds	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	20.0%–80.0%
Voluntary pension funds	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	20.0%–80.0%

Note: Benchmark porfolios are rebalanced annually.

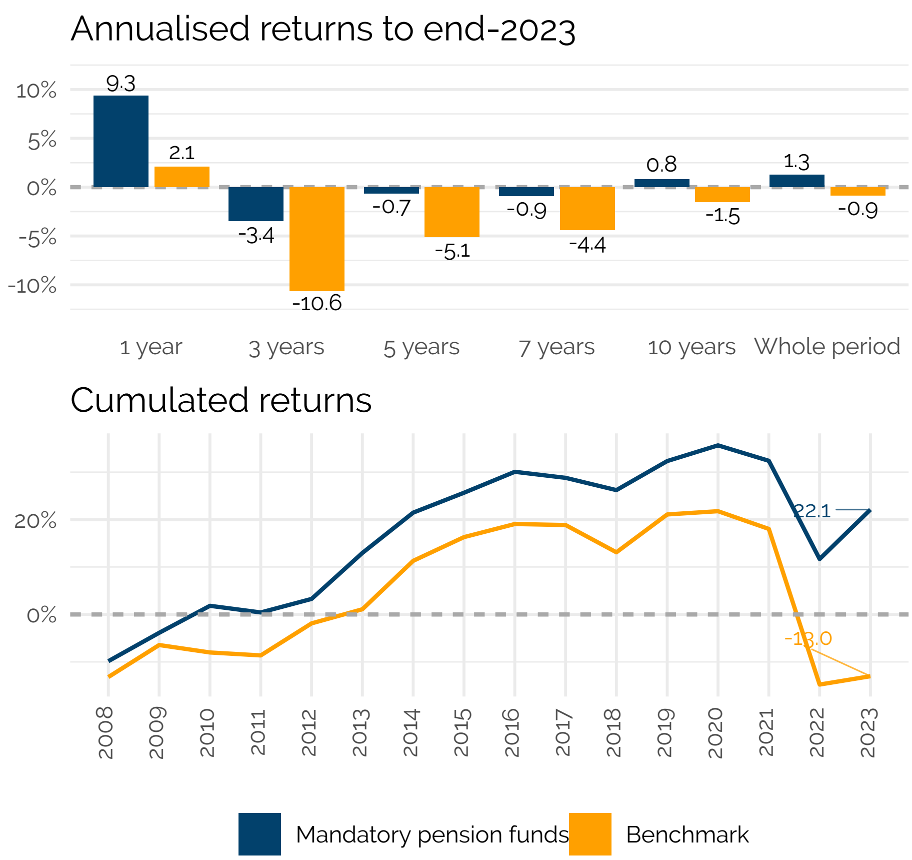
Pillar II Mandatory pension funds do perform quite strongly compared to the capital market benchmark. Detailed evolution of the performance of pension funds are presented in Figures RO.9 and RO.10.

While the respective market benchmark has been negative on the analysed timeframe 2008–2023, Romanian mandatory pension funds were able to beat the benchmark and keep the real value of savings of the analysed period.

The different story is being seen when comparing the performance of Romanian voluntary pension funds with the respective market benchmark.

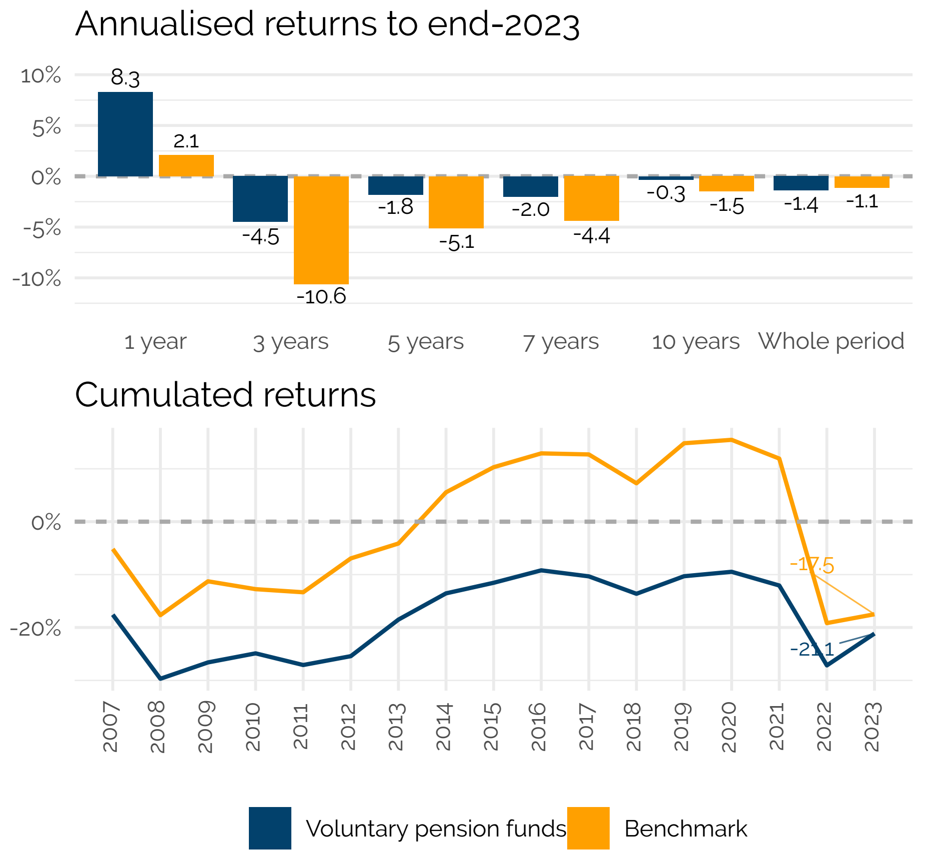
Over the analysed period of 2007–2023, the cumulative performance of the Pillar III pension funds was below its market benchmark and also negative. The key element explaining the results seems to be the high level of charges as the portfolio composition is quite similar to Pillar II funds.

Figure RO.9 – **Performance of Romanian mandatory pension funds against a capital market benchmark (returns before tax, after inflation, % of AuM)**



Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE, holding periods to end-2

Figure RO.10 – Performance of Romanian voluntary pension funds against a capital market benchmark (returns before tax, after inflation, % of AuM)



Data: ASF Romania, Eurostat; *Calculations:* BETTER FINANCE, holding periods to end-2

Conclusions

Romania's population is rapidly decreasing and ageing, which—unless they adopt the necessary reforms—will lead to the explosion of the demographic bomb in a few decades. In the public PAYG pensions system, the state collects contributions from employees and redistributes the money among existing pensioners. Demographics show that this redistribution logic is no longer viable, as contributors' numbers will fall, and the number of pensioners is already going up. The departure from this dilemma takes the form of the private pensions system, allowing each active person to save for their own future retirement.

Romanian pillar II is a fully funded system based on personal accounts and on the DC philosophy. Pillar II is mandatory for all employees aged under 35 years and voluntary (optional) for employees aged 35 to 45. The starting level of contribution was set at 2% of the participant's total gross income and increases by 0.5 percentage points annually until it reaches 6 of total gross income in 2017. However, this level has not been reached, and the contribution system has reversed.

Mandatory pension funds are managed by their administrators—PMCs. Each PMC is obliged by respective law to administrate and manage just one mandatory pension fund. Currently, there are seven PMCs managing seven mandatory funds on the Romanian Pillar II market. The market is dominated by two PMCs (AZT and NN) and as the portfolio structure of pension funds are quite similar, there is no real competition among providers and no viable life-cycle investment strategy is applied.

Romanian pillar III is also a fully funded system based on personal accounts and on the DC philosophy. Pillar III represents privately managed supplementary pensions. This system is opened to all income cohorts. Voluntary pension funds in Pillar III are managed by their administrators—PMCs, LICs or AMCs. Each administrator is obliged to establish and operate at least one voluntary pension fund. Currently, there are eight providers offering 10 voluntary pension funds. Pillar III market is fairly concentrated, where three dominant players cover almost 90 of the market.

Mandatory as well as voluntary pension funds' investment strategy is strictly regulated. The law imposes percentage limits and restrictions for different asset classes. It must be noted that investment rules in mandatory and voluntary system are very similar. This fact logically causes implications on portfolio structure, thus also on performance of mandatory and voluntary pension funds in Romania. Currently about 73% of all investments in Pillar II as well as Pillar III pension funds are bond investments (Romanian Government Money market instruments and Bonds) and only about 22 is invested in equities, which could raise a question about suitability of portfolio structure with regard to the age structure of savers.

Overall, the real return of pension funds in Pillar II is positive, however high charges weight on the performance of Pillar III pension funds. Combining the effect of high fees and low participation, the Pillar III needs a serious reform in order to play an important role in securing adequate pension income for savers in a future.

References

Badea, D. G., & Novac, L. E. (2007). The evolution of pension funds on the romania market. *Review of Management and Economical Engineering*, *6*(6).

Cenar, I. (2010). The financial - accounting image for the public benefits of retiretment. *Annals of the University of Petroşani, Economics*, *10*(3), 51–60. Retrieved October 26, 2023, from https://www.upet.ro/annals/economics/pdf/annals-2010-part3.pdf#page=51

Frunzaru, V. (2007). *Romanian pension system: An evaluation from the European Perspective*. Economic Publishing House.

Muntean, L., & Stanciu, A.-P. (2011). Deductibility of contributions to voluntary private pensions. *Annals of the University of Petroşani, Economics*, *11*(4), 215–222. Retrieved October 26, 2023, from https://www.upet.ro/annals/economics/pdf/annals-2011-part4.pdf#page=215

The writing and publication of this report is co-funded by the European Union. There is no implied endorsement by the EU or the European Commission of work carried out by BETTER FINANCE, which remains the sole responsibility of BETTER FINANCE.