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Earnings-related pension assets reached EUR 215 billion at the end of 2019

The earnings-related pension system is in part financed by investment assets. During 2019, these assets increased by approximately EUR 21 billion, totalling EUR 215 billion at the end of December. The increase in assets was due to the exceptionally favourable development of equity investments during the year. At the same time, the return on fixed-income investments was also excellent, owing to continually lower interest rates.

Analyst **Kimmo Koivurinne's** analysis of the trend in earnings-related pension assets comprises the following sections:

- Return on investments nominally 12.5 per cent in 2019
- Year of the Bull 2019
- Basic facts about our investment statistics

Return on investments nominally 12.5 per cent in 2019

- Investment assets of the earnings-related pension system, in total: EUR 215 billion (*)
    - Investment assets in the private sector: EUR 135 billion
    - Investment assets in the public sector: EUR 81 billion
- Growth in the final quarter of the year: about EUR 6 billion
- Investments in equities and equity-like instruments accounted for EUR 106 billion, or 49 per cent of all investment assets
- Fixed-income investments: EUR 73 billion, share 34 per cent
- Real estate investments: EUR 18 billion, share 9 per cent
- Alternative investments: EUR 18 billion, share 8 per cent
- Returns on investments for the whole year 2019: 12.5 per cent nominally and 11.5 per cent in real terms.

(*) On 31 December 2019, the investment assets of earnings-related pension providers totalled approximately EUR 216 billion. The amount of investment assets presented here differs from the figure in the financial statements by almost one billion. The reason lies in different statistical processes. We will specify the amount of assets during the spring.

In investment distribution, the relative shares of the various asset categories changed slightly during 2019. The share of fixed-income investments (34%) diminished by 4 percentage points. The share of equities and equity-like instruments [1] (19%) increased by 5 percentage points. The share of real estate investments (8%) remained virtually unchanged, while the share of alternative investments [2] (8%) diminished by less than one percentage point. In the longer term, i.e. in the 2010s, the relative share of fixed-income investments shrank by about ten percentage points. Fixed-income investments

have been replaced by better performing equities, private equity and hedge funds. The underlying factor is the prolonged low interest rate level, which has led earnings-related pension providers to seek replacement investments within the framework of the solvency regulations. In the light of the returns, this strategy seems to have worked well.
[1] When the analysis refers to investments in equities and equity-like instruments, this means the following categories of investment figures: quoted shares (incl. equity funds) and other investments in equities, which include, for instance, private equity and investments in unquoted shares.

[2] In general, alternative investments refer to hedge funds.

The regional distribution of investments changed little during the past year. The shares of domestic investments and euro area investments each fell by about one percentage point. The relative share of investments outside the euro area increased by about two percentage points. At the end of the year, less than a quarter of investment assets (23%) was invested in Finland, less than one fifth (18%) elsewhere in the euro area, and more than half (59%) in countries outside the euro area. Changes in the relative shares of investments are affected by net flows — that is, the difference between purchases, sales and maturities.

The longer-term strategy has been to diversify investments increasingly into the global investment market. Over the past decade, the share of domestic investments in pension portfolios has fallen from 35% in the early 2010s to less than a quarter. At the same time, the share of investments in the rest of the euro area has also shrunk from 31% to less than a fifth. On the other hand, the share of investments outside the euro area has risen from 34% at the beginning of the decade to almost 60%.

For the whole year of 2019, the **returns** of the six largest operators **in each investment category** were as follows:

- Average returns on equity investments: 21.5 per cent in nominal terms and 20.4 per cent in real terms
- Average returns on fixed-income investments: 5.5 per cent in nominal terms and 4.5 per cent in real terms
- Average returns on real estate investments: 7.6 per cent in nominal terms and 6.6 per cent in real terms
- Average returns on alternative investments: 3.5 per cent in nominal terms and 2.6 per cent in real terms

The trend of returns on pension investments must be examined over the longer term; changes occurring during one quarter — or even during a year — are not of major importance to the financial sustainability of the pension system. In addition, future returns cannot be predicted on the basis of the returns realized. Over the long term, in the end, the pension assets put into funds for the future pension liabilities increase in step with economic growth and inflation. It should be noted that the selection of the examination period is also important. The effect of the review interval on average return is illustrated by comparing the average returns of 20 and 23 years.

The returns realized look steady in the longer term:

- 2015–2019 (5 years): 5.6 per cent in nominal terms and 4.9 per cent in real terms
- 2010–2019 (10 years): 6.1 per cent in nominal terms and 4.7 per cent in real terms
- 2000–2019 (20 years): 5.0 per cent in nominal terms and 3.6 per cent in real terms
- 1997–2019 (23 years): 5.9 per cent in nominal terms and 4.3 per cent in real terms

The real return used by the Finnish Centre for Pensions for its long-term projections is 2.5 per cent until 2028. Thereafter, the projected real return is 3.5 per cent. The latter projection has been used to examine the pension system all the way until 2085. Then the big picture depends the most on trends in employment, the birth rate and net immigration.

Pensions are financed not only by pension contributions but also by investment assets placed into funds and the subsequent returns. In addition, since 2014, the private sector's investment assets in funds have been affected by the fact that the pensions paid out of the funds and their returns have exceeded the sum of pension contributions placed into the funds. According to preliminary calculations, in 2019, the entire pension sector collected EUR 2.7 billion of pension contributions into funds, while the sum taken out for pensions paid totalled EUR 4.5 billion. This means that the net sum used for pensions from funds and their returns totalled EUR 1.8 billion.

Thanks to the good returns on investments in 2019, the solvency of pension insurers is strong. The solvency ratios of the four largest pension insurance companies at the end of December ranged between 124.4 and 130.8 per cent. Solvency positions ranged between 1.6 and 2.0. Solvency ratios and positions did not change notably over the past year. Thanks to the buffers meant for rainy days, pension insurers are also able to withstand worse periods on the financial market.

Year of the Bull 2019

According to the Chinese horoscope, last year was the Year of the Pig. In terms of investments, however, 2019 was the Year of the Bull. The bull symbolizes the power of the rising market. In fact, a statue of the bull has been erected in the centre of the financial world, Wall Street in New York. The Year of the Bull 2019 began under favourable conditions in the sense that any slack in stock prices had been eliminated by a sharp decline in the last quarter of the previous year. Thus, a good foundation had been laid for the recovery of stock values at the outset of the year, as soon as uncertainty would dissipate. At the beginning of the year, the U.S. Federal Reserve gave its support to the market and announced that it would take a timeout before any interest hikes. This was to the stock market's liking, and returns on domestic pension investments also showed a yield of over five per cent in the first quarter.

In the second quarter of the year, the bogeyman on the market was again the trade war between China and the United States. Despite the trade war, equities — especially in developed markets — performed very well, even though the stock market adopted a risk-averse position for a while around

May–June. However, the positive attitude of the central banks supported the market, and the key stock indices closed the quarter on a positive note.

In the third quarter of last year, economic indicators showed deceleration of growth. However, central banks on both sides of the Atlantic acted as guardians of the market. The generous monetary policy helped equities in the developed world to retain their value despite slimmer economic forecasts. The prolonged setting of competing import tariffs between China and the United States dimmed the global economic outlook. The declining interest rate level on the market, in line with expectations, made fixed-income investments perform very well even though the atmosphere in the emerging stock markets was far from perfect.

Brexit, which had chafed Europe in particular, was confirmed towards the end of the year. At the same time, the United States and China reached a kind of truce in the trade war, which put the finishing touches to an investment year that had already been excellent. Major international stock indices closed last year with returns of well over twenty per cent, while fixed-income investments also yielded excellent returns. This marked the end of a decade that brought very good returns, especially on equity investments.

- The S&P 500 index, describing the stock market performance of the five hundred largest U.S. companies, rose by as much as 28.9 per cent per year after the fall in stock prices in 2018.
- The German DAX index also rose more than 25 percent. The FTSE index, which describes the development of the 100 largest companies on the London Stock Exchange, remained at 12 per cent after Brexit had been confirmed.
- The OMXH25 index, which describes the development of the largest companies on the Helsinki Stock Exchange, rose in the wake of the world market by 14.6 per cent during the year.
- During the same period, the OMXS30 index of the Stockholm Stock Exchange gave a better yield: over 25 per cent during the past year.
- The record low interest rate level also boosted fixed-income investments, which produced the best annual return of the decade.

Basic facts about our investment statistics

Our member organizations are responsible for investing the statutory earnings-related pension assets. The statistics cover the pension insurance companies, the TyEL funds of industry-wide pension funds and company pension funds, as well as the public-sector earnings-related pension providers: Keva, the State Pension Fund (VER), the pension liability fund for employees of the Social Insurance Institution Kela, the Church Pension Fund (KER) and the Bank of Finland’s Pension Fund (SPERA). Also included is the group of specialized pension providers, which comprises the Farmers’ Social Insurance Institution (Mela) and the Seafarers’ Pension Fund (MEK).

The statistics only cover the statutory earnings-related pension assets put into funds. They do not include the value of the collective supplementary pension funds managed by industry-wide pension funds and company pension funds, which was approximately EUR 4.3 billion at the end of 2019.