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Economic Restructuring in Post Conflict Countries:

The case of Oil and Pension Funds

Stephen Lewarne
Executive Vice President
TSG Inc.

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Oil Funds: Intended Purposes

- Given the large sums involved, it is important that investment and oversight institutions and procedures be chosen that are suitable for the intended purpose
 - Revenues could be universally shared among the whole population
 - Revenue sharing could evolve into needs-based social assistance, once capacity is built within the government to make needs assessments in an accurate, transparent, efficient, non-discriminatory manner
 - Revenues could be used for capital improvements and infrastructure projects
 - Revenues could form a fund for the purpose of investment for development. In this case, revenues would be invested and expected to earn a return
 - All capital should be held as investments for income and growth and should be managed using international best practices

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Oil Funds: Options

- It is useful to look at models in other countries:
 - The Norwegian Petroleum Fund is considered to be the world’s best managed petroleum fund, with strong institutions and international best practices to manage investments. (Investments are all held outside the country, intended to benefit the population over the long-term).
 - The Alaska Petroleum Fund is an example from the US. The Kuwaiti Petroleum Fund is a relatively good model from the region.
 - The Saudi experience of using petroleum revenues to fund education and infrastructure projects has been successful
 - Azerbaijan has a petroleum fund much like Norway’s—in theory but is subject to severe abuse and “capital-bleeding.”
- In my experience it is essential to choose the Norwegian model (if politically acceptable), and then make plans to have in place a solid fiscal authority with international best practice fiscal governance policies (procurement, treasury systems, budget processes, current and capital spending synchronized etc.)

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Pension Funds: Options

- Pension funds in many ways are similar to petroleum funds
- often, pension fund and petroleum fund managers attend the same conferences and follow the same principles of governance and investment
- Good models of pension funds from international practice include:
 - The Canadian Pension Fund
 - The Irish Pension Fund
 - The New Zealand Pension Fund
 - the Kosovo Pension Savings Trust
- For post conflict economies I prefer the Kosovo model, for the same reason as with petroleum funds- if invested offshore in a balanced portfolio, it will provide a long-term stream of income that will outlast cyclical problems of re-building government

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Pension Funds: Kosovo a brief Outline

- The old system was a typical East European system with very high contribution rates, frequent delays in payment of pensions, a high level of evasion by contributors, early retirement ages, special categories of earlier retirement, a complicated benefit formula, and increasing financial unsustainability
- The new system had two components:
- The first component in the system provides an old-age “basic pension” (paid to all Kosovars, 65 years of age and older) and a disability pension, both of which are funded from general revenues rather than an earmarked wage tax. Pensions are paid through the banking system rather than through the postal service, reducing administrative costs. The disability pension is narrowly focused on total and permanent disability, ensuring that scarce resources are well focused on the truly disabled.

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Pension Funds: Kosovo a Brief Outline

- The second component of the system is a mandatory, defined-contribution, savings pension program.
- The program requires all working, habitual residents of Kosovo to contribute 5% of gross salary, matched by a 5% employer contribution.
- Contributions and records are managed by the Kosovo Pension Savings Trust (KPST), an independent body with strong governance and supervision, established solely for the purpose of administering the savings component of the pension system.
- The KPST invests participants' assets on their behalf.
- Very high standards are set to ensure security of pension investments at the same level of safety enjoyed by other European citizens for their pension investments.
- Several Governing Board members are “representative” of Kosovo society, while the majority of Board members must have strong “professional” experience, meeting criteria that would be required for a trustee by any major European pension fund that follows good investment practices.
- These high standards also necessitate investment abroad at present, at least until Kosovo’s domestic financial markets are much more developed.
- Strong governance processes and top-quality Governing Board members who meet high international professional standards are critical for ensuring safe long-term guardianship of participants' pension assets.
- The process of collecting contributions is centralized to minimize administrative fees.



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Kosovo Pension Fund: Success

- The reform has achieved a number of important policy outcomes.
- The Basic Pension helps avoid high payroll taxes since there is no wage-based “social contribution”—it is funded from the general budget.
- The modest contribution to funded pension accounts, coupled with an absence of other payroll taxes and low personal income taxes, should avoid labor-market distortions that have affected many other countries.
- In this way, the system is conducive to job creation and economic growth.
- The Basic Pension achieves near universal coverage of all elderly over 65 in an environment where only a small share of the population earns formal wage income, in contrast to the old Yugoslav system that reached only approximately half of Kosovo’s elderly.
- The Basic Benefit is tied to the cost of a basic monthly food basket, linked to official government statistical surveys, in order to contain long-term costs with a real anchor.
- This long-term fiscal sustainability leaves enough fiscal room for other important needs-based social programs rather than crowding out such programs.
- The system adheres to a principle of clear division of roles, where the first component ensures poverty avoidance and the second component serves as the main vehicle for savings.
- Funds under the second component are securely invested according to international best practices, and already are returning positive real net returns to participants, with comparatively low administrative fees.
- The foundation for supervision of mandatory and voluntary funded pensions is strong, with effective transparency requirements.



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