



NATIONAL BANK OF SERBIA

**INSURANCE SUPERVISION DEPARTMENT
PENSION FUNDS SUPERVISION DIVISION**

VOLUNTARY PENSION FUNDS IN SERBIA

Second Quarter Report 2014

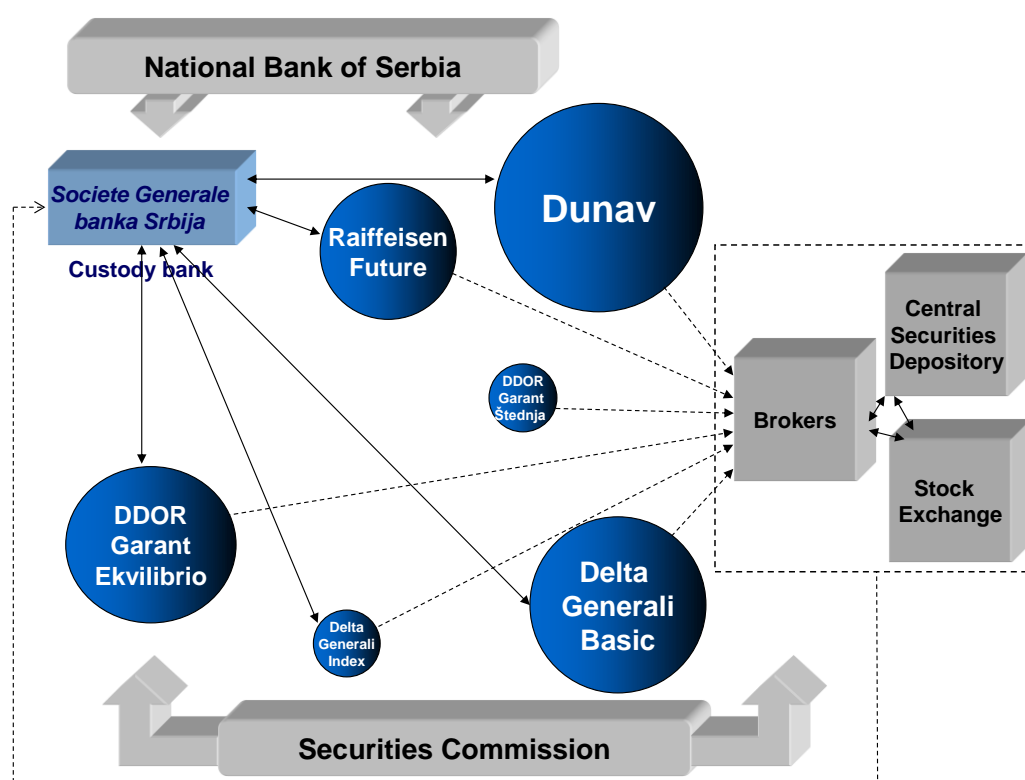
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1. Market participants

At end-Q2 2014, the market of voluntary pension funds (VPFs) comprised four companies managing six VPFs, one custody bank and four agent banks¹.

Market participants



At end-Q2, total employment in VPF management companies was 129, up by one relative to the previous quarter.

By late Q2 2014, there were 496 sales agents licensed by the NBS, based on completed professional examination and the fulfilment of other requirements, to disseminate information about VPF operation.

By the end of the quarter observed, there were 75 sales agents engaged by management companies and 191 by intermediary banks.

¹ NLB bank a.d. Belgrade, Raiffeisen bank a.d. Belgrade, Sberbank a.d. Belgrade and Societe Generale bank Srbija a.d. Belgrade.

2. VPF net assets

At end-Q2 2014, net assets came to RSD 21.7 billion, up by 5.5% quarter-on-quarter or 20.5% year-on-year. The value of net assets changes on account of net contributions², withdrawals and the return on investment. In the

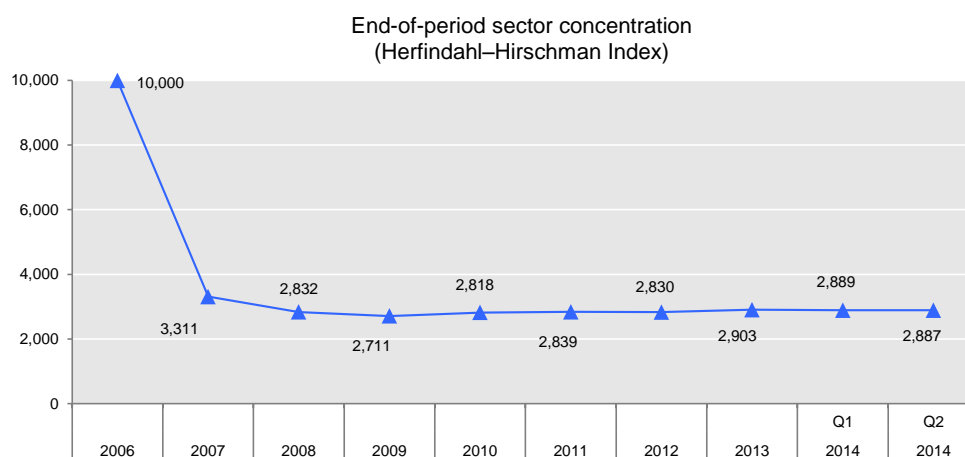
quarter reviewed, net assets expanded rather because of the return on investment than because of net contributions exceeding withdrawals. In Q2 2014, total and net contributions amounted to RSD 671.1 million and EUR 658.1 million respectively. Withdrawals totalled RSD 299.3 million and return on investment RSD 781.3 million.

Net assets amounted to RSD 21.7 billion, up by RSD 1.1 billion relative to the quarter before.

End-of-period net assets of the VPF sector
(in RSD bln)

2007	2008	2009	2010	2011	2012	2013	2014	
							Q1	Q2
3.1	4.6	7.2	9.9	12.5	16.0	19.7	20.6	21.7

Source: National Bank of Serbia.



Source: National Bank of Serbia.

Measured by HHI, market concentration³ in the sector remained high – 2,887 points at end-Q2. According to the size of VPF net assets relative to net sector assets, two funds were classified as “large” and “medium”, making up over 97% of the market, while the largest fund accounted for around 42%.

² Net contributions are total contributions minus the front-load fee.

³ In terms of the share in total net assets.

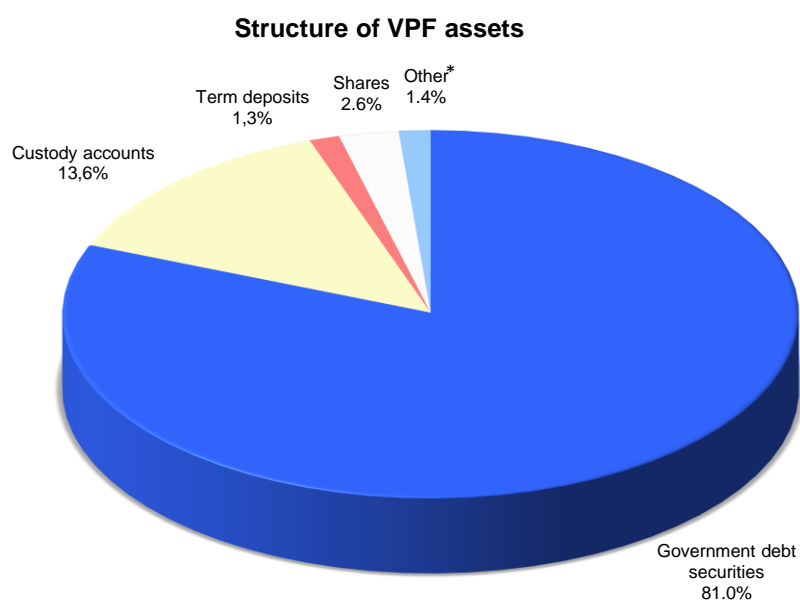
Number of funds by groups divided by market share (in units)									
Share in net assets (%)	2007	2008	2009	2010	2011	2012	2013	2014	
								Q1	Q2
Large (20 and above)	3	2	2	3	2	2	2	2	2
Medium (5 - 19,99)	-	2	3	1	2	2	2	2	2
Small (0 - 4,99)	4	6	5	4	5	5	2	2	2

Source: National Bank of Serbia.

3. Structure of VPF net assets

At end-Q2 2014, the structure of VPF net assets remained broadly unchanged. Government debt securities still accounted for the major portion of VPF assets – 81.0%, of which government bonds made up 80.3% (including frozen FX savings bonds – 0.96%), and T-bills – 0.7%. Balances in custody accounts and term deposits made up 14.9% and shares 2.6% of total VPF assets.

Most assets were invested in government debt instruments – around 81.0% (average maturity – around 3.5 years).

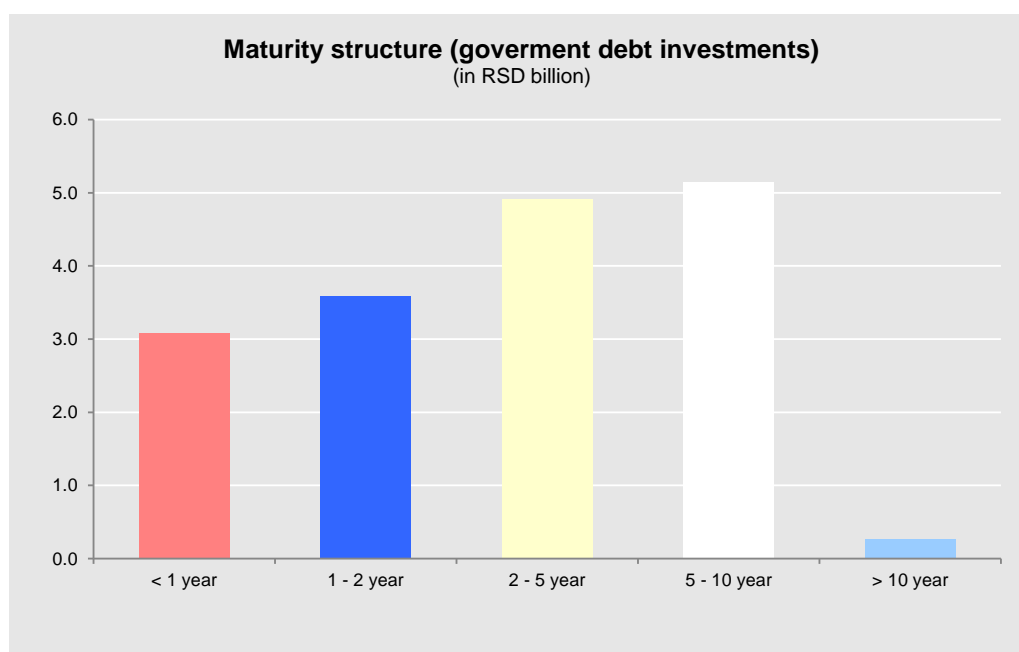


Source: National Bank of Serbia.

* Other assets include: corporate bonds, real estate, investment units of open-end investment funds and claims.

At end-Q2 2014, the maturity structure of government debt instruments was as follows: 18% with the maturity of up to one year, 21% with the maturity of one–two years, 29% with the maturity of two–five years, 30% with the maturity of five–ten years, and 2% with the maturity over 10 years.

The average maturity⁴ of assets invested into government debt instruments was around 3.5 years. At end-Q1 2014, the average maturity of these assets was around three years.



Dinar assets made up around RSD 18.5 billion or 85.1%, while foreign currency assets accounted for RSD 3.2 billion or 14.9% (13.4% in EUR and 1.5% in USD).

4. Return on investment

At end-Q2 2014, FONDex⁵ reached 1,973 points⁶. The return of FONDex, which represents the weighted average return of all funds, came at 3.8% in Q2, while the return for the last year measured 10.7%. Since the start of VPF operation⁷, the return of FONDex equalled 9.3%.

Given the structure of VPF investment, the return is under the influence of a change in the yield curve on government debt instruments⁸ (changes in interest rates of

⁴ The maturity of instruments weighted by their share in total investment in government debt instruments.

⁵ FONDex shows movements in investment units of all VPFs in the market.

⁶ The initial FONDex value of 1,000 points was recorded on 15 November 2006 when the first VPF began to operate.

⁷ Annual rate.

⁸ A decline in the interest rate impacts on an increase in prices of debt instruments and vice versa. Prices of longer-maturity instruments are more sensitive to interest rate changes.

some maturities), changes in prices of shares, the level of the key policy rate and banks' interest rates, and changes of the dinar exchange rate against the euro.

An increase was recorded for the volume of issues in the primary market of government debt instruments (T-bills and government bonds) relative to the previous quarter, while discount rates went down.

The total market value of dinar-denominated issues came at RSD 90.5 billion in Q2 vs. RSD 83.6 billion in the previous quarter. Most issued were one-year (RSD 24.4 billion), two-year (20.3 billion) and three-year (15.7 billion) instruments. Also issued were three-month, six-month and one-year T-bills (total RSD 36.8 billion), as well as two-, three-, five- and seven-year bonds (total RSD 53.7 billion).

Market value of issued dinar-denominated government debt instruments, by maturity (in RSD bln)					
Maturity	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014
3m	2.9	9.8	6.0	5.9	6.9
6m	5.6	2.9	5.7	2.9	5.5
12m	20.4	17.9	20.4	27.1	24.4
18m					
24m	20.0	15.8	12.1	18.5	20.3
36m	11.8	3.3	29.6	22.2	15.7
60m	1.2	0.4	4.6	3.0	4.0
84m	3.1	0.6		4.1	13.7
Total	65.0	50.5	78.5	83.6	90.5

Source: Ministry of Finance.

In the period observed, the accepted rates on dinar instruments declined relative to the previous quarter.

Accepted rate of issued dinar-denominated government debt instruments, by maturity					
Maturity	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014
3m	9.2%	9.2%	9.1%	7.5%	7.6%
6m	9.1%	9.4%	9.0%	7.8%	7.7%
12m	9.1%	10.8%	9.4%	8.9%	8.2%
18m					
24m	9.9%	11.5%	10.1%	9.8%	9.0%
36m	10.5%	12.0%	10.2%	10.5%	10.0%
60m	10.5%	10.7%	11.9%	11.5%	10.8%
84m	12.3%	13.0%		13.0%	11.8%

Source: Ministry of Finance.

The period reviewed also saw the issue of euro-denominated government debt instruments worth around EUR 424.1 million – one-year (EUR 113.2 million) at a 3.2% rate, two-year (EUR 128.6 million) at a 4.1% rate, three-year (EUR 62.8 million) at a 4.7% rate, five-year (EUR 23.9 million) at a 4.9% rate, and ten-year (EUR 96.6) at a 5.5% rate. Interest rates declined relative to the previous quarter.

Market value of issued euro-denominated government debt instruments, by maturity (in RSD bln)					
Maturity	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014
12m	29.2	-	130.5	48.4	113.2
24m	50.3	50.0	138.2	68.5	128.6
36m	33.9	37.2	-	49.6	62.8
60m	42.4	25.8	60.0	47.3	23.9
120m	-	-	-	-	96.6
Total	155.7	113.0	328.7	213.8	424.1

Source: Ministry of Finance.

Accepted rate of issued euro-denominated government debt instruments, by maturity					
Maturity	Q2 2013	Q3 2013	Q4 2013	Q1 2013	Q2 2014
12m	3.2%	-	3.5%	3.3%	3.2%
24m	4.2%	4.5%	4.3%	4.1%	4.1%
36m	4.5%	5.0%	-	4.8%	4.7%
60m	5.0%	5.3%	5.2%	5.1%	4.9%
120m	-	-	-	-	5.5%

Source: Ministry of Finance.

At end-Q2 2014, yields on frozen FX savings bonds ranged from 3.6% for A2015-series to 3.8% for A2016-series. The 2014-series bonds matured on 16 May 2014. Compared to the quarter before, yields increased by 43 and 24 basis points respectively.

Prices of Belgrade Stock Exchange (BSE) shares, measured by BELEX15⁹, rose 1.0% in Q2 (vs. 569.8 by end-June). The index gained 18.7% over the last year.

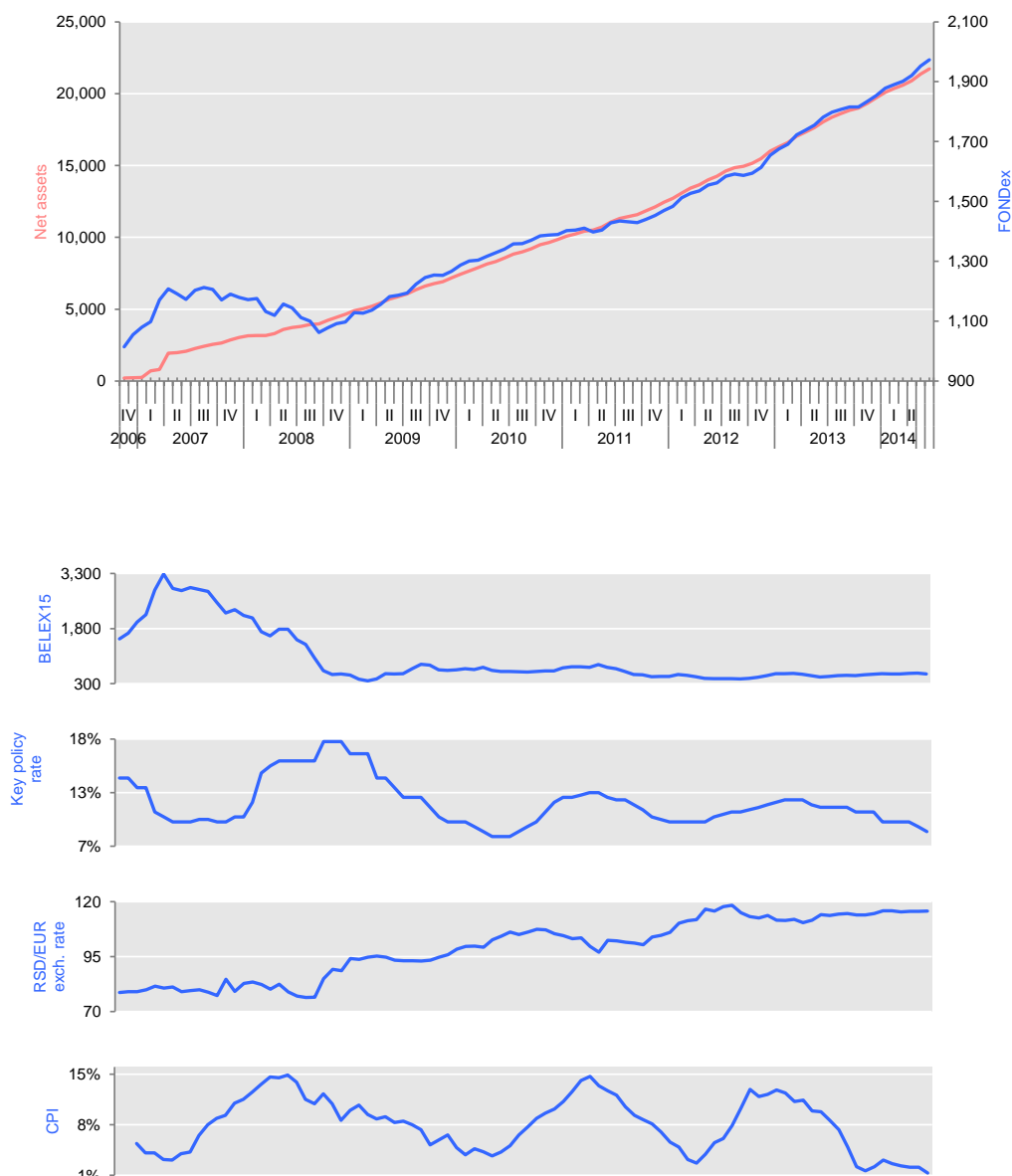
The key policy rate was cut to 8.5% from the previous quarter. The interest rates earned by funds on dinar balances in custody accounts mirrored movements in the key policy rate.

In Q2, the exchange rate of the dinar was stable relative to the euro – the dinar depreciated by 0.3% compared to end-Q1 2014. In the same period, the dinar lost 1.1% against the US dollar.

Inflation slowed down in Q2. Monthly growth rates came at 0.6%, 0.1% and 0.1% in April, May and June, respectively. CPI went up 1.3% in June 2014 year-on-year.

⁹ Of total investment in shares, the bulk pertained to shares covered by BELEX15, which means that BELEX15 is a relevant benchmark for shares in the funds' portfolio.

Movements in net assets, FONDex and key indicators since the start of VPF operation
(in RSD mln, units, %)



Source: National Bank of Serbia, Belgrade Stock Exchange, Statistical Office

5. Fees charged by management companies

The Law on Voluntary Pension Funds and Pension Schemes sets out maximum fees that may be charged to fund members. Contribution and management fees may not exceed 3% and 2% of the accounting net value of assets respectively, while the account transfer fee may be charged only at the level of real transfer costs.

Management fees will be limited to 1.25% once net assets of all funds reach 0.75% of GDP.

The new Law, adopted in early May 2011, envisages different fees charged by management companies – these fees will be applied once net assets of all funds reach 0.75% of GDP. The maximum management fee is set at 1.25%, while the contribution fee is not capped. VPF net assets accounted for around 0.56%¹⁰ of GDP.

Fees are one of the parameters that members should bear in mind when choosing a fund, but should not be observed as an isolated factor. The fee level is contingent on the fund investment strategy and its performance. As a rule, more active funds, intended for younger persons who pay contributions over a longer horizon, invest in more complex instruments to a higher extent and assume greater risk, which is why they are expected to post higher return. However, they also charge higher fees. On the other hand, a fund investing passively in safer financial instruments should charge lower fees. Investment policy, i.e. scheduled investment by fund members, the expected fund return, the risk taken by a fund (and a member), and fees charged by companies, should be taken into account when opting for a fund.

Since the start of operation, companies charged a 2.0% management fee, while the contribution fee was cut to 1.9% on average in Q2 2014. The relative proportion of the two fees reversed – at the start of VPF operation, contribution fees were dominant by contrast to the current 89% of management fees. This was a result of a rising net asset value and an enlarged base to which management fees are applied.

In Q2 2014, the average contribution fee was 1.9%.

Though visible in the first instance, the contribution fee is not the largest cost incurred by a member. It is paid only once, as a front-load fee.

The management fee is charged every day on the value of VPF net assets and is contained directly in the investment unit value, meaning that the calculated and published value is deduced by the amount of the management fee.

In Q2 2014, the management fee equalled RSD 105.1 million, while the return on investment totalled RSD 781.3 million. Over the past year, the fee equalled RSD 393.8 million and the profit reached RSD 2,045.2 million. A further rise in net assets and boosted fund competition may result in gradual lowering of the management fee.

¹⁰ Source: GDP – database of the Serbian Statistical Office, quarterly GDP at current prices, seasonally non-adjusted data.

Fees charged by management companies (in RSD mln)									
	2007	2008	2009	2010	2011	2012	2013	2014	
								Q1	Q2
Contribution fee	42.9	56.9	54.9	59.4	57.9	60.1	58.7	12.7	13.0
Management fee	37.8	73.5	117.3	170.7	220.0	284.1	357.8	99.6	105.1

Source: National Bank of Serbia.

6. Trading in securities

VPF trading volumes equalled RSD 8.4 billion in Q2 2014.

On the purchase side, the major part related to auctions of government debt instruments. The share of VPFs in BSE trading was around 4.3% vs. 2.3% in the quarter before.

VPF securities trading (in RSD bln)								
	2008	2009	2010	2011	2012	2013	2014	
							Q1	Q2
Securities trading	1.7	13.1	14.9	19.3	13.2	12.9	4.5	8.4
Purchases	1.8	8.1	8.1	10.6	7.1	9.0	2.9	3.7
Belgrade Stock Exchange	0.8	0.4	1.3	0.7	0.3	0.4	0.1	0.8
Unregulated market	0.3	0.4	0.3	1.3	0.1	0.7	0.0	0.5
Auctions of government securities	0.0	7.3	6.5	8.6	6.7	7.9	2.8	3.2
Sales	0.4	0.4	0.8	3.8	4.2	2.0	1.1	2.0
Belgrade Stock Exchange	0.1	0.1	0.6	0.4	0.3	0.6	0.1	0.2
Unregulated market	0.3	0.3	0.2	3.4	3.9	1.4	1.1	1.8
Maturity	0.2	4.6	6.1	4.9	2.0	2.0	0.5	2.6
Purchase to sale and maturity ratio	2.4	1.6	1.2	1.2	1.1	2.3	1.8	0.8
Share in total BSE trading (in%)	1.2%	1.1%	8.0%	3.8%	2.6%	3.4%	2.3%	4.3%

Source: National Bank of Serbia, Belgrade Stock Exchange.

7. Transaction costs

Transaction costs incurred in the purchase, sale and transfer of securities (Central Securities Depository fees, stock exchange fees, tax charges) and costs of the current maintenance of property that fund assets are invested in are charged against fund assets. Other costs are incurred by management companies (brokerage and custody bank fees).

Central Securities Depository fees, charged against VPF assets, accounted for the largest portion of transaction costs, whereas the costs paid by management companies from their assets, these being brokerage and custody bank fees, made up the bulk of costs paid from VPF assets.

Amount of transaction costs (in RSD mln)									
	2007	2008	2009	2010	2011	2012	2013	2014	
								Q1	Q2
Total	10.0	5.3	7.4	9.5	7.0	4.7	6.0	1.6	1.8
Brokerage fees	4.5	2.2	3.8	4.5	2.9	2.0	2.5	0.5	0.7
Custody bank fees	1.8	1.5	2.0	2.4	2.2	1.5	1.9	0.4	0.5
Stock exchange fees	1.6	0.8	0.4	1.1	0.8	0.3	0.6	0.1	0.2
Central Securities Depository fees	1.0	0.6	1.2	1.5	1.1	0.9	0.9	0.5	0.4
Transfer tax relating to the acquisition of securities	1.1	0.2	-	-	-	-	0.1	-	0.0

Source: National Bank of Serbia.

8. Number and structure of VPF users

At end-Q2 2014, 185,712 users¹¹ were in the accumulation phase¹². Total membership contracts stood at 250,102¹³.

Total number of users was 185,712 at end-Q2 2014.

Number of contracts and users (in thousand)									
	2007	2008	2009	2010	2011	2012	2013	2014	
								Q1	Q2
No. of contracts	158.5	201.6	215.7	220.4	234.4	240.4	244.5	250.4	250.1
No. of users	-	155.95	165.2	166.8	174.9	179.8	183.5	185.8	185.7
Percentage of active users (in %)	-	41.6%	36.0%	43.9%	35.1%	30.5%	30.3%	27.7%	29.7%

Source: National Bank of Serbia.

VPF users accounted for around 2.5% of the total population. Each tenth employee was a VPF member.

The amount of accumulated funds per user depends on the amount of contributions, the funds' return, level of fees, and the length of the accumulation phase. With an increase in the level of contributions and the period of accumulation, alongside the returns, the amount of average balances in members' individual accounts

¹¹ The number of users is the number of members of one or more VPFs. The number is smaller than the number of membership contracts as a significant number of users have more than one membership contract in one or several funds.

¹² VPF membership has two phases – the accumulation phase (when contributions are made) and the withdrawal phase (when the accumulated funds are withdrawn).

¹³ The number of membership contracts is the sum total of individual membership contracts and the number of members of all pension schemes.

increases. The average amount of accumulated funds of members who have made at least one contribution was somewhat above RSD 139,000 and is constantly rising.

Structure of users by payment dynamics (in units and %)			
	Period	No. of users	Share (%)
Active users	1 month	55,131	30%
	3 months	61,909	33%
	6 months	65,549	35%
	12 months	77,593	42%
	From the start of membership (1)	156,193	84%
	No holdings (2)	29,519	16%
	Total (1+2)	185,712	

Source: National Bank of Serbia.

At end-Q2 2014, the number of members of two or more VPFs amounted to 35,639 or 19.2% of the total.

Average accumulated funds at the period-end (in RSD thousand)								
2007	2008	2009	2010	2011	2012	2013	2014	
							Q1	Q2
-	34.6	52.2	70.5	84.5	105.3	127.3	131.3	139.1

Source: National Bank of Serbia.

**Number of users by
number of funds in which
they are members**
(in units)

No. of funds	No. of users
1	150,073
2	26,156
3	9,407
4	73
5	1
6	2

Source: National Bank of Serbia.

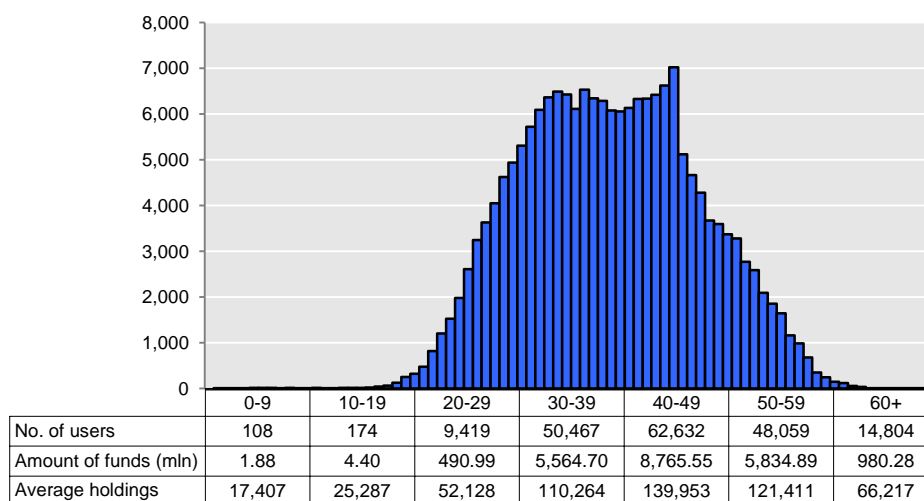
**Number of users by
membership contract**
(in units)

No. of contracts	No. of users
1	138,596
2	33,678
3	10,610
4	2,098
5	529
6	148
7	38
8	6
9	9

Source: National Bank of Serbia.

In terms of gender composition, no significant changes were recorded relative to previous years. Men remained dominant with around 60%.

Distribution of users and accumulated funds by age
(in units, RSD)



Source: National Bank of Serbia.

At end-Q2 2014, the average age of VPF users was around 45 years, while users aged 30–50 accounted for around 61%. Such user structure has not changed since the start of VPF operation. Further, the percentage of users above the age of 53 was similar to previous years, accounting for around 23% of the total.

9. Contribution payments, withdrawals and transfers

Apart from 2007 when most VPFs were set up and when contributions were the lowest, total contributions were stable throughout the years, ranging between RSD 2.2 and 2.7 billion a year.

Contribution payments came at RSD 671 million in Q2 2014.

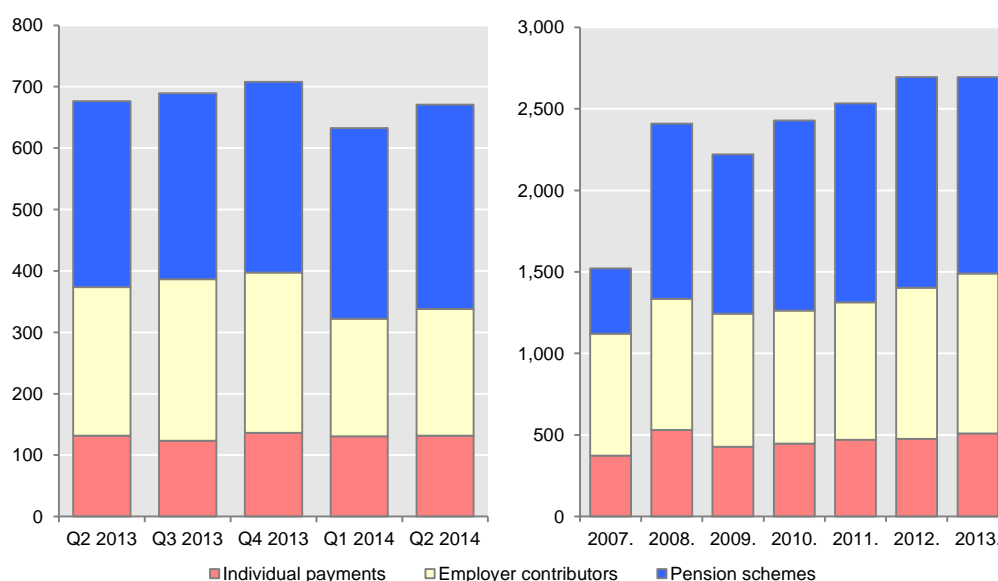
In Q2 2014, of total contributions, individual payments accounted for 19.6%, employer contributions 30.8% and pension plans 49.6%. This ratio has been broadly unchanged since 2008.

Total contributions (in RSD bln)

2007	2008	2009	2010	2011	2012	2013	2014	
							Q1	Q2
1.52	2.41	2.22	2.43	2.53	2.7	2.70	0.63	0.67

Source: National Bank of Serbia.

Volume and structure of total contributions
(in RSD mln, %)



Source: National Bank of Serbia.

Though the Law envisages individual contributions, most are made through employers that thus show a high degree of responsibility towards their employees. Ample potential for further growth in the membership base are companies with high staffing levels. Contributions by individuals and employees up to a specified amount are exempt from the household income tax and contributions for mandatory social insurance. The non-taxable contribution amount is set at RSD 5,329¹⁴ per employee per month. Payments in the same amount made by the employer through wage garnishment and payments from employee wages are also tax-exempt. This represents an additional incentive to employees and employers to direct a part of contributions to saving in VPFs.

Withdrawals are generally lump-sum. Though this contradicts the nature of VPFs which assumes the use of accumulated funds over a longer period, such practice of withdrawal is expected as members entitled to withdrawal are not long-standing fund members and their accumulated sum is therefore relatively small. Further period is likely to see an increase in scheduled and other types of withdrawals, in response to growth in accumulation years and the accumulated sum. Moreover, members who joined VPFs after the Law was amended in May 2011 are entitled to maximum lump-sum withdrawal of 30%.

Total withdrawals (in RSD mln)								
2007	2008	2009	2010	2011	2012	2013	2014	
							T1	T2
141.4	384.6	448.5	458.1	517.6	751.7	945.2	252.5	299.3

Source: National Bank of Serbia

¹⁴ Under the Government decree, this amount is adjusted with previous-year inflation once a year.

Withdrawals grow by the year as a result of system development – as contributions and net assets increase and the third pillar matures, absolute withdrawals will rise as well.

In Q2 2014, total withdrawals amounted to RSD 299.3 million.

Transfers represent inter-fund transfers. A member may for any reason decide to transfer a part or all of his/her assets from one fund to another, and he/she has to cover only real transfer costs.

In Q2 2014, total withdrawals amounted to RSD 20.9 million.

Total inter-fund transfers
(in RSD mln)

2007	2008	2009	2010	2011	2012	2013	2014	
							Q1	Q2
19.5	235.1	141.5	216.1	165.9	72.3	137.2	57.2	20.9

Source: National Bank of Serbia.