

CHILE-EXTRACT GUIDE TO LATIN AMERICA PENSIONS INVESTMENT CONTEXT AND REGULATIONS –

The Guide complements the work done by Campollo Consulting LLC and Wall's Street Advisors Services LLC on Pensions Funds across 11 countries in Latin America, their asset allocation, returns and authorized investment products

*A source to the
region's Pensions
Investment Practices
and Regulators*

Jan 2012

Chile – Pension Funds' Investment Context and Regulations

About Campollo Consulting LLC – Campollo Consulting LLC, a minority owned firm, was established by Carmen Campollo. Over the past 20 years Carmen has worked for firms such as the World Bank, International Finance Corporation, Standard & Poor's, FTSE and Russell Investments. In addition to the Guide for Pension Funds Investment Context and Regulations, Campollo Consulting has developed a data base for 11 Latin American countries, including a 5 year history of asset allocation across 23 categories for over 400 pension funds. In addition Campollo Consulting created a methodology for manager searches for Emerging Markets, an Index Multistrategy Fund of Funds, and developed financial products. You can learn more about Campollo Consulting at www.campolloconsulting.com

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Chile – Pension Funds’ Investment Context and Regulations

Chile has three types of approaches to pension fund asset management, each with its own set of investment regulations and policies:

- Management companies called Administradores de Fondos de Pensiones (AFPs), where individuals direct their mandatory contributions into one of a series of funds (called *multifondos*) they select. Each multifondo allocates assets on risk-based criteria. Each AFP (there were 6 operating as of end-Dec. 2011) offers 5 funds, called respectively A, B, C, D, and E Fund, with A Funds offering the most aggressive asset allocation and E Funds the most conservative mix. The AFPs’ *multifondos* represent by far the largest amount of Chilean pension assets.
- Voluntary contribution accounts, which were introduced under *Ley de Reforma el Sistema Previsional* (Ley 20255) of March 2008, may be added to the contributor’s AFP Fund account or may be invested in a self-directed form with other asset managers such as banks, mutual funds, and insurance companies. These are reported so far to not represent a significant amount of assets, and unless contributed to one of the AFP funds, are not subject to any specific investment regulation. (The management companies however are subject to fiduciary laws and regulations).
- A sovereign wealth fund, called the Fondo de Reserva de Pensiones (FRP), which ‘back-stops’ the national social security system. The FRP receives an annual allocation between 0.2% and 0.5% of GDP from the national government (depending on the size of Chile's overall budget surplus each year), is administered by the Central Bank on behalf of the Ministry of Economy (Hacienda), and is managed on a day-to-day basis by a committee of experts appointed by the Central Bank. Established in 2006, the FRP by law cannot begin to disburse funds for ten years from its establishment.

The AFP System – Key Institutions and Regulations

The AFP system was established by Decree Law 3500 (1980), which continues in effect as subsequently amended. The system was modified under *Ley de Reforma el Sistema Previsional* (Ley 20255) of March 2008, to introduce the *multifondos* concept. The *Regimen de Inversion de los Fondos de Pensiones* (last modified with effect from January 31, 2012), issued by the Superintendencia de Pensiones, delineates the responsibilities of the parties of the AFP investment process and the most recent investment parameters for AFP *multifondos*.

The major institutions involved in the asset-management side of the AFP system are the AFPs themselves; their immediate regulator the Superintendencia de Pensiones (Supen); the Consejo Tecnico de Inversiones (CTI, Technical Council on Investments); the Central Bank; the

Superintendencia de Valores y Seguros (SVS, Superintendency of Securities & Insurance); and the Comision Clasificadora de Riesgo (CCR, Commission for Risk Classification).

The AFPs are specialized companies formed to administer pension accounts on behalf of their clients. They are shareholder-owned companies whose shares must be listed on the Chilean stock exchange. As such, they are subject to all the exchange’s listing requirements and to the laws and regulations governing public companies, as enforced by the SVS.

The Supen has direct responsibility for overseeing all the activities of the AFPs and the funds in their care, and as far as their asset management practices go, for issuing and revising the Regimen de Inversion and enforcing compliance.

The CTI is a high-powered committee responsible for making broad recommendations to Supen about what constitutes eligible investment categories for AFP multifondos. Its 5 members are appointed by the President of the Republic (1 member), the Central Bank (1), the AFPs collectively (1), and the deans of accredited universities with economic and/or economic and administration programs (2 members).

The Central Bank (BC) is also involved in determining the structural limits of investment categories across the aggregate AFP system and for determining eligible secondary markets, foreign and domestic credit ratings services, foreign custodians, risk factors of domestic financial institutions, and other aspects of investment management that may affect the AFP system.

The CCR determines the risk qualities of foreign mutual funds and foreign investment funds, and of other foreign securities. It may also solicit classifications on its behalf.

The Fondo de Reserva de Pensiones (FRP)

The FRP was established under Ley 20128 (Sept. 2006). Its investment regulations technically are the same as those applied to the AFP funds under DL 3500, but its policies are governed by its own investment committee, and the fund is administered by the Central Bank.

From inception until early 2012, the resources of the FRP have been invested in low-risk asset classes, similar to the investment portfolio of the country’s international reserves. The strategic asset allocation included sovereign bonds (66.5%), money market instruments (30%), and government bonds indexed to inflation (3.5%). The reference currency composition was 50% in U.S. dollars, 40% in Euros, and 10% in Japanese yen, though instruments in other currencies which have liquid hedging markets are eligible.

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In late 2010, the Investment Committee decided to expand the eligible asset categories and currencies to include global equities and corporate bonds. In December 2011, the Central Bank completed the selection of external managers who will be responsible for managing global equity portfolios (up to 15% of assets) and corporate bond portfolios (up to 20% of assets).

The Central Bank chose BlackRock Institutional Trust Company, NA and Mellon Capital Management Corporation for the portfolio of stocks, and BlackRock Institutional Trust Company, NA and Rogge Global Partners Plc for the portfolio of corporate bonds, from among 40 candidates. In addition, the Inflation-linked Sovereign Bonds category's target allocation will increase to 15%.

The Money Market and Sovereign Bonds (Nominal) categories' target allocations will shrink to 5% and 45% of total assets, respectively, to accommodate the new asset classes' allocations.

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Chile - AFP Table A: Structural Investment Limits (in terms of AFP fund value) *

* Summarized from Regimen de Inversion's article III.1

Instrument	Fondo A		Fondo B		Fondo C		Fondo D		Fondo E	
	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges	Limit Ranges
	Minimum	Maximum	Minimum	Maximum	Minimum	Maximum	Minimum	Maximum	Minimum	Maximum
Issued by the Treasury, Central Bank MINVU, Bonos de Reconocimiento, & other national securities	30%	40%	30%	40%	35%	50%	40%	70%	50%	80%
Foreign Investment Aggregated Limits: Foreign instruments + indirect investment abroad through mutual funds	Minimum 30% funds' value (A+B+C+D+E); Maximum 80% funds' value (A+B+C+D+E)									
Limit by Fund:	45%	100%	40%	90%	30%	75%	20%	45%	15%	35%
Investment in foreign currencies without exchange cover	30%	50%	25%	40%	20%	35%	15%	25%	10%	15%
	Limit of Fund B > Fund C > Fund D > Fund E									
Restricted Securities: illiquid shares + securities not approved by the CCR + private sector securities w/maturities under 3 years & rated below BBB & N-3 or have less than 2 ratings	10%	20%	10%	20%	10%	20%	10%	20%	0%	0%
Equities (domestic & foreign) & other instruments that represent capital & which have been publicly offered and fall under the SVS or SBIF	40%	80%	25%	60%	15%	40%	5%	20%	0%	5%
	Fund A > Fund B > Fund C > Fund D > Fund E									

Source: Superintendencia de Pensiones; Regimen de Inversion de los Fondos de Pensiones, January 2012; www.safp.cl/573/articulos-7749_reg_inv_FP.pdf

Chile – Pension Funds’ Investment Context and Regulations

Chile - AFP Table B: Limits by Instrument & Groups of Instruments (in terms of AFP fund value) *

* Summarized from Regimen de Inversion's article III.2

Instrument	Fondo A Limit Ranges Maximum	Fondo B Limit Ranges Maximum	Fondo C Limit Ranges Maximum	Fondo D Limit Ranges Maximum	Fondo E Limit Ranges Maximum
Bonds of public & private enterprises convertible to shares (domestic & foreign)	30%	30%	10%	10%	3%
Operations or contracts of loans or participations in financial instruments in letter m) - domestic	15% of domestic investments	15% of domestic investments	15% of domestic investments	15% of domestic investments	15% of domestic investments
Operations or contracts of loans or participations in financial instruments in letter m) - foreign	1/3 of foreign assets	1/3 of foreign assets	1/3 of foreign assets	1/3 of foreign assets	1/3 of foreign assets
Restricted Securities: illiquid shares + securities not approved by the CCR + private sector securities w/maturities under 3 years & rated below BBB & N-3 or have less than 2 ratings	20%	20%	20%	20%	0%
Outstanding subscription payments and payment into investment fund shares	2%	2%	2%	2%	2%
Every type of instrument in letter K	1%	1%	1%	1%	1%
Total sums used as margins for derivatives in letter I in article II.1, distinct from clearing houses	2% domestic 2% foreign 3%	2% domestic 2% foreign 3%	2% domestic 2% foreign 3%	2% domestic 2% foreign 3%	2% domestic 2% foreign 3%
Operations involving derivatives outlined in letter I.2 in article II.1	Measurement of exposure: total exposure in the asset subject to all relevant limits, minus the 'funding' for debt instruments				
Overnight & Time Deposits with foreign banks	2%	2%	2%	2%	2%
Currency Hedging using currency denomination in the case of mutual funds and investment securities, certificates based on financial indices, and other instruments defined by the SP	50% of the value of the investment in foreign currency	50% of the value of the investment in foreign currency	50% of the value of the investment in foreign currency	50% of the value of the investment in foreign currency	50% of the value of the investment in foreign currency

Source: Superintendencia de Pensiones; Regimen de Inversion de los Fondos de Pensiones, January 2012; www.safp.cl/573/articles-7749_reg_inv_FP.pdf

The Guide to Latin America Pension Funds

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Chile - External Managers Data

Chilean AFPs do not publicly disclose their external asset management arrangements; FRP has not external managers to date. The regulator does get info on the ten largest equity funds and fixed income funds by total assets are specified; the 24 asset management companies with the most AuM at 12/2011 (of 40

Asset Type	Pension Fund's Project Code ---> Manager/Product Name	CHL001.1	CHL001.2	CHL001.3	CHL001.4	CHL001.5	CHL002.1	CHL002.2
		Capital - A	Capital - B	Capital - C	Capital - D	Capital - E	Cuprum - A	Cuprum - B
Equity	BlackRock iShares S&P 500 Index Fund	5	5	5	5	5	5	5
Equity	Fidelity - China Focus Fund	5	5	5	5	5	5	5
Equity	Fidelity South-East Asia Fund	5	5	5	5	5	5	5
Equity	Franklin Templeton Asian Growth Fund	5	5	5	5	5	5	5
Equity	Gartmore SICAV - Latin America Fund	5	5	5	5	5	5	5
Equity	Fidelity Funds - Latin America Fund	5	5	5	5	5	5	5
Equity	BlackRock iShares MSCI Emerging Markets Index	5	5	5	5	5	5	5
Equity	SSgA SPDR S&P 500 ETF Trust	5	5	5	5	5	5	5
Equity	Vanguard Emerging Markets Index Funds	5	5	5	5	5	5	5
Equity	Vanguard Total Stock Market Index Fund	5	5	5	5	5	5	5
Fixed Income	Axa World Funds - US High Yield Bonds	5	5	5	5	5	5	5
Fixed Income	BlackRock Global - US Dollar High Yield Bond	5	5	5	5	5	5	5
Fixed Income	BNP Paribas L1 - World Bond Emerging Local	5	5	5	5	5	5	5