

INDIVIDUAL PENSION SYSTEM 2023

RISK INVENTORY



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Message from Senior Management

With the painful consequences of two major earthquakes in February 2023 centered in Kahramanmaraş, we were reminded once again about the value of an effective national, industrial, and institutional risk management framework.

In the last few years, the problems caused by the COVID-19 pandemic, elevated inflation, supply chain crises, energy security risks, the Ukraine-Russia war, and geopolitical conflicts have come to the fore as major global issues. While global trends raise the possibility that economic risks, such as inflation and high cost of living, will remain topical in the short and medium term, surveys show that external environmental risks like the climate change, natural hazards, and ecological collapse may take precedence in the long run.

It is also highly probable that such developments will

directly affect individual pension systems. While the fluctuations in the financial markets and the changes in the income-consumption-savings patterns of individuals since the emergence of the COVID-19 pandemic are very likely to put heavy strain on individual pension systems in the coming period, the need for pension companies to have strong governance and healthy risk management strategies is estimated to be greater than ever.

The surveys conducted for this report reveal the importance of “protecting savings from inflation.” To that end, creating an ecosystem where pension mutual funds will provide stable real returns is essential.

We would like to take this opportunity to thank all our industry stakeholders for their valuable contributions to our efforts.

Sincerely,

MUSTAFA AKMAZ

CEO

ULUÇ İÇÖZ

CHAIRMAN





Executive Summary

Risks were identified based on the evaluations of our stakeholders' internal systems units. This year, five new risks were added to the inventory: the effects of high inflation and the regulations on the victims of delayed pension age (EYT) on the industry, loss of key personnel, the industry's inability to obtain a competent and qualified workforce, and the failure to maintain geopolitical stability.

The electronic survey designed by the PMC was distributed to the target audience of 604 people consisting of relevant specialists and managers in stakeholder institutions, and 48 percent completed the survey. The summary profile of survey respondents is presented in Appendix 2.

Survey participants were asked to evaluate 70 risks

on a scale of 1 to 10, and the rankings of risks were determined based on the risk severity calculated by multiplying impact and probability. The top 10 risks are included on pages 6, 7 and 8 of the report.

The devastating earthquake that occurred on February 6, 2023, deeply affected our industry and the entire country, as we were reminded about the possibility of earthquakes once again. This was also reflected in this year's survey results, as "natural hazard risk" ranked first in the inventory for the very first time.

This year, external environmental risks related to the economy were prioritized across the industry as they were across the world. Meanwhile, the challenges experienced in the supply of labor were reflected in the evaluations, and human resources risks ranked high.

Substantial Risks According to Survey Respondents

The inventory focuses on the individual pension industry.

The risks identified and agreed upon with the evaluations of the units responsible for the internal systems of pension companies were presented to the survey participants and rated by them in terms of impact and probability on a scale of 1 to 10.

Risks by Severity (Impact x Probability)

The risks included in the survey were sorted based on risk severity calculated by multiplying the impact and probability values provided by survey respondents. The resulting top 10 risks are listed below. The previous years' results are also shown.

Rankings marked with “-” indicate new risk definitions that were not included in the previous year's inventory.

Table 1 – Top 10 Risks by Risk Severity (Impact x Probability)

2023 Rankings	2022 Rankings	2021 Rankings	Risk Definition	Risk Type
1	6	8	Natural hazard risks	EXTERNAL
2	1	2	Impact of potential fluctuations in the economy on new contract entries	EXTERNAL
3	-	-	Savings not reflecting the expected real growth due to high inflation	PORTFOLIO MANAGEMENT
4	5	4	Perception of lower returns compared to alternatives	PORTFOLIO MANAGEMENT
5	4	1	Potential improvements and changes in state incentives to the system	STRATEGIC
6	2	-	Exchange rate risk	EXTERNAL
7	12	7	Insecurity and investment costs stemming from frequent changes in system design and legislation	STRATEGIC
8	8	3	Relative insufficiency of retirement income from the system and negative perceptions of the system	PORTFOLIO MANAGEMENT
9	-	-	Potential inability to attract a competent and qualified workforce	STRATEGIC
10	3	-	Risk of widespread poverty	EXTERNAL

Risks by Impact Level

Risk definitions were sorted based on respondent evaluations of the impact level on a scale of 1 to 10. The top 10 risks are presented in Table 2. The rankings of these risks in the previous years are provided in the table.

Rankings marked with “-” indicate new risk definitions that were not included in the previous year’s inventory.

Table 2 – Top 10 Risks by Impact Level

2023 Rankings	2022 Rankings	2021 Rankings	Risk Definition	Risk Type
1	4	9	Natural hazard risks	EXTERNAL
2	-	-	Savings not reflecting the expected real growth due to high inflation	PORTFOLIO MANAGEMENT
3	3	2	Perception of lower returns compared to alternatives	PORTFOLIO MANAGEMENT
4	6	8	Impact of potential fluctuations in the economy on new contract entries	EXTERNAL
5	2	1	Potential improvements and changes in state incentives to the system	STRATEGIC
6	9	11	Reputational risks for companies and the system	STRATEGIC
7	6	6	Risk of operating license revocation or bankruptcy for pension companies	STRATEGIC
8	8	10	Risk of damage to system infrastructures as a result of cyber attacks	INFORMATION TECHNOLOGIES
8	12	7	Risk of sudden outflow of funds	STRATEGIC
9	13	5	Relative insufficiency of retirement income from the system and negative perceptions of the system	PORTFOLIO MANAGEMENT
10	11	-	Risk of widespread poverty	EXTERNAL

Risks by Degree of Probability

Risk definitions were sorted based on respondent evaluations of the degree of probability on a scale of 1 to 10. The top 10 risks are presented in Table 3. The rankings of these risks in the previous years are provided in the table.

Rankings marked with “-” indicate new risk definitions that were not included in the previous year’s inventory.

Table 3 – Top 10 Risks by Degree of Probability

2023 Rankings	2022 Rankings	2021 Rankings	Risk Definition	Risk Type
1	1	1	Impact of potential fluctuations in the economy on new contract entries	EXTERNAL
2	12	5	Natural hazard risks	EXTERNAL
3	-	-	Savings not reflecting the expected real growth due to high inflation	PORTFOLIO MANAGEMENT
4	2	-	Exchange rate risk	EXTERNAL
5	8	7	Perception of lower returns compared to alternatives	PORTFOLIO MANAGEMENT
6	13	4	Insecurity and investment costs stemming from frequent changes in system design and legislation	STRATEGIC
7	7	2	Potential improvements and changes in state incentives to the system	STRATEGIC
8	-	-	Potential inability to attract a competent and qualified workforce	STRATEGIC
9	3	-	Risk of widespread poverty	EXTERNAL
10	6	3	Relative insufficiency of retirement income from the system and negative perceptions of the system	PORTFOLIO MANAGEMENT

Notes on Risk Definitions in Tables

Natural hazard risks

Türkiye is prone to earthquakes and natural hazard such as earthquakes, floods, landslides, storms, tornadoes, and fires directly affect firms' business continuity, service provision capacity, income, and financial structure in all industries, including the individual pension system. Similarly, they may also impact the economy and human behavior, potentially reducing the amount people allocate to savings and prompting the early withdrawal of individual pension system savings.

Impact of potential fluctuations in the economy on new contract entries

This refers to the risk of lower amounts of funds available for savings and the withdrawal of current individual pension system savings to fulfill urgent cash needs against high inflation, rising commodity prices and other effects observed in Türkiye and all around the world due to the pandemic.

Savings not reflecting the expected real growth due to high inflation

The risk that the returns of pension mutual funds will remain below the inflation rate, rendering the participants' savings unable to beat inflation.

Perception of lower returns compared to alternatives

It is known that returns obtained in the system are often compared to widely used investment tools such as deposits, gold and foreign exchange without consideration of factors such as risk level, risk appetite and differing payments.

This comparison feeds the perception that returns in the system are lower than other investment tools and, as financial literacy is substantially lower in Türkiye like it is in the rest of the world, this perception might discourage participation in the system while encouraging current participants to withdraw from the system.

Potential improvements and changes in state incentives to the system

This refers to the impact of the improvement in the state incentives provided to the system on the industry's growth, collection rates and the system reaching a wider audience. With the amendment of the Law on January 22, 2022, the state contribution was increased from 25 to 30 percent. Just like the previous years, the industry views potential improvements and changes in state incentives as major leverages.

Exchange rate risk

This refers to the indirect risk of exchange rate fluctuations influencing the amount people allocate to savings especially since the end of 2021 and the more direct risk of them choosing foreign currency and FX-protected deposit accounts over the individual pension system for investment purposes.

Insecurity and investment costs stemming from frequent changes in system design and legislation

Previous changes and turning points in the individual pension system including the state contribution, structural changes in deduction, and the auto-enrollment system are significant factors to consider for industry managers, as the subsequent infrastructure changes inflict costs and impact short- and medium-term corporate projections and expectations.

Relative insufficiency of retirement income from the system and negative perceptions of the system

As the individual pension system is contribution-based, the retirement income from the system depends on the contribution amount and its returns. Participants may be dissatisfied if they made payments (widely) disproportionate to their expected pension income during their accumulation period and therefore could not receive the amount they expected in retirement. Their expression of this dissatisfaction through various communication channels might negatively impact others who lack basic information about the system.

Potential inability to attract a competent and qualified workforce

This refers to the risks of the industry's inability to attract and retain human resources in line with the new set of competencies shaped by the changing ways of doing business, new technologies and needs, and therefore being unable to exhibit the expected innovative approaches.

Risk of widespread poverty

This refers to the risks of financial difficulties reducing the amounts that can be put aside by individuals as savings and the use of current savings for primary needs in line with the global trend that is expected to continue to gain momentum.

Reputational risks for companies and the system

This refers to the risks of adverse events in pension companies or the industry affecting the reputation of companies and the entire industry, and the effects of this loss of reputation on growth expectations.

Risk of operating license revocation or bankruptcy for pension companies

While lower in probability thanks to firm supervision and audit mechanisms, this risk focuses on the possible impact on industry growth and potential damage to the perception of reliability of other companies in the industry rather than on direct consequences to participants, as participant funds are kept separate from corporate assets in individual accounts at Istanbul Settlement and Custody Bank.

Risk of damage to system infrastructures as a result of cyber attacks

This is a growing threat induced by process digitalization and remote working practices and is considered a substantial risk as it might impact service continuity in all industries, including the individual pension system, and the potential to damage industry reliability.

Risk of sudden outflow of funds

This risk includes the potential impact on the pension companies of collective withdrawals from the system as well as negative consequences on the fund's investment strategy, and accordingly, the returns for ongoing participants.

Conclusion and Assessment

Natural Hazard Risk Takes First Place

Due to the devastating earthquake on February 6, 2023, centered in Kahramanmaraş, which affected 10 provinces in the country, the Istanbul earthquake is back on the agenda. While natural hazard risk ranked sixth and eighth in previous years, it took the first place in this year's survey.

7 of the Top 10 Risks Consist of External and Strategic Risks

Seven of the top 10 risks consist of external risks arising from the economic crisis (widespread poverty, increasing exchange rates, potential fluctuations in the economy) and anticipation of natural hazards.

The Risk of Access to a Competent Workforce is Now in the Top 10

This year, the risk of the industry's inability to attract a competent and qualified workforce was ranked in the top 10. It would not be wrong to say that the current difficulties in reaching the right person and promotion are effective in the risk assessments of the managers. The challenges faced in accessing human resources compatible with this changing skill set, in qualified workforce not choosing the relevant industry and in the failure to retain this qualified workforce were ranked as a major risk in terms of achieving company and industry goals in the following periods.

External Risks Rank Higher in Internal Systems Units

Compared to the employees of the other units, the risks defined as "loss of key personnel" by the personnel working in the internal systems were defined much higher and were included in the top 10. It is noteworthy that risks such as geopolitical instability and climate change were once again prioritized compared to other units.

Variety of Issues on Senior Management Agenda

It was observed that the risks of collection failures and talent management were the main items on the senior management agenda. The change in the skill set and the challenges in accessing qualified workforce affect the pension industry just like every other industry.

Perception of Risk Increases in Participants with Vast Industry Experience Due to Legislation Changes

Survey participants with 10 or more years of working experience in the industry placed the risks of insecurity and investment costs stemming from frequent changes in legislation among the top 10 risks, while the participants who have just started working in the industry ranked this risk 13 to 14 times lower.

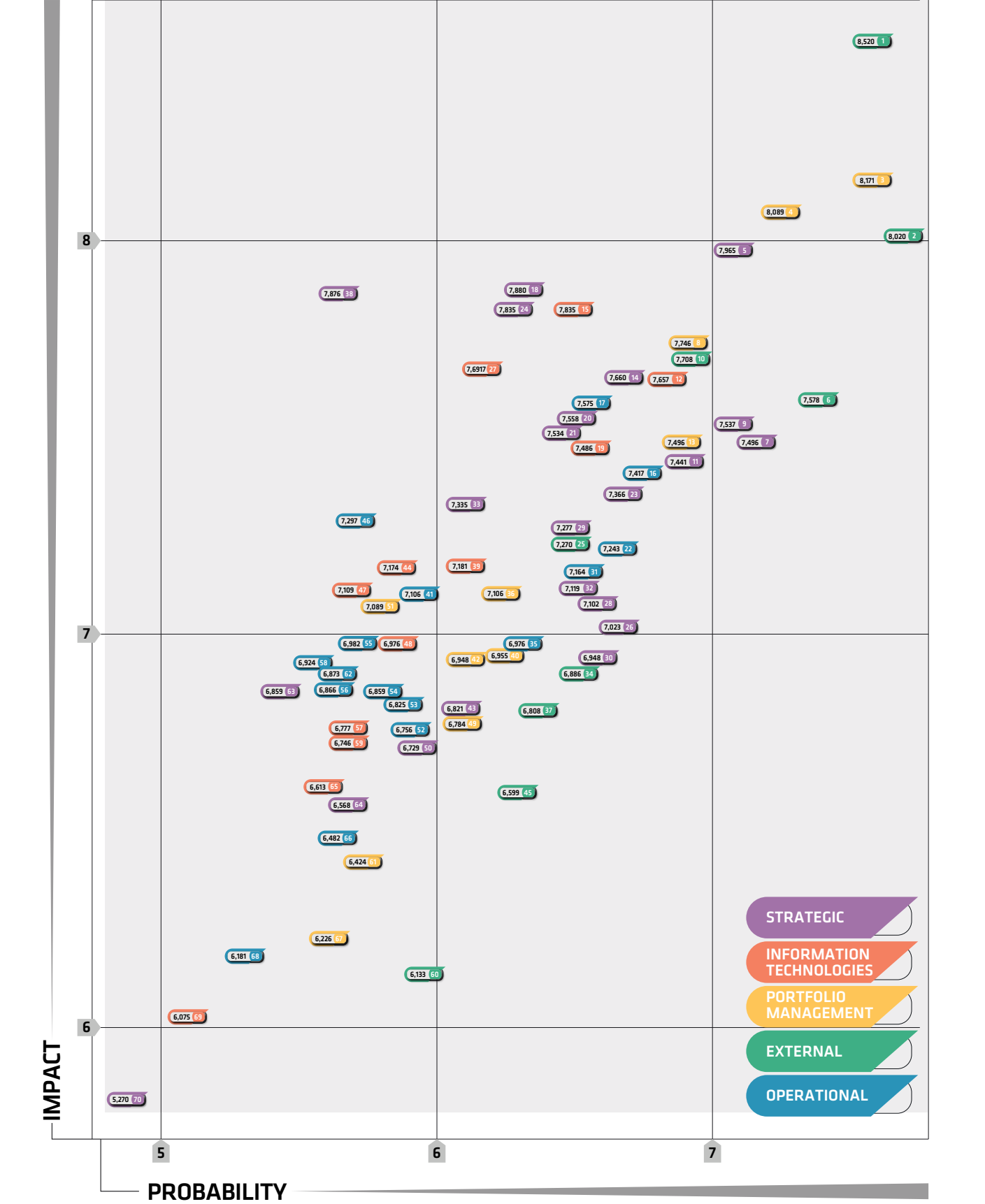
Operational Risks Ranked Lower

There is no operational risk among the top 15 risks. Operational risks lag far behind in terms of impact and probability when compared to strategic and external economic risks.



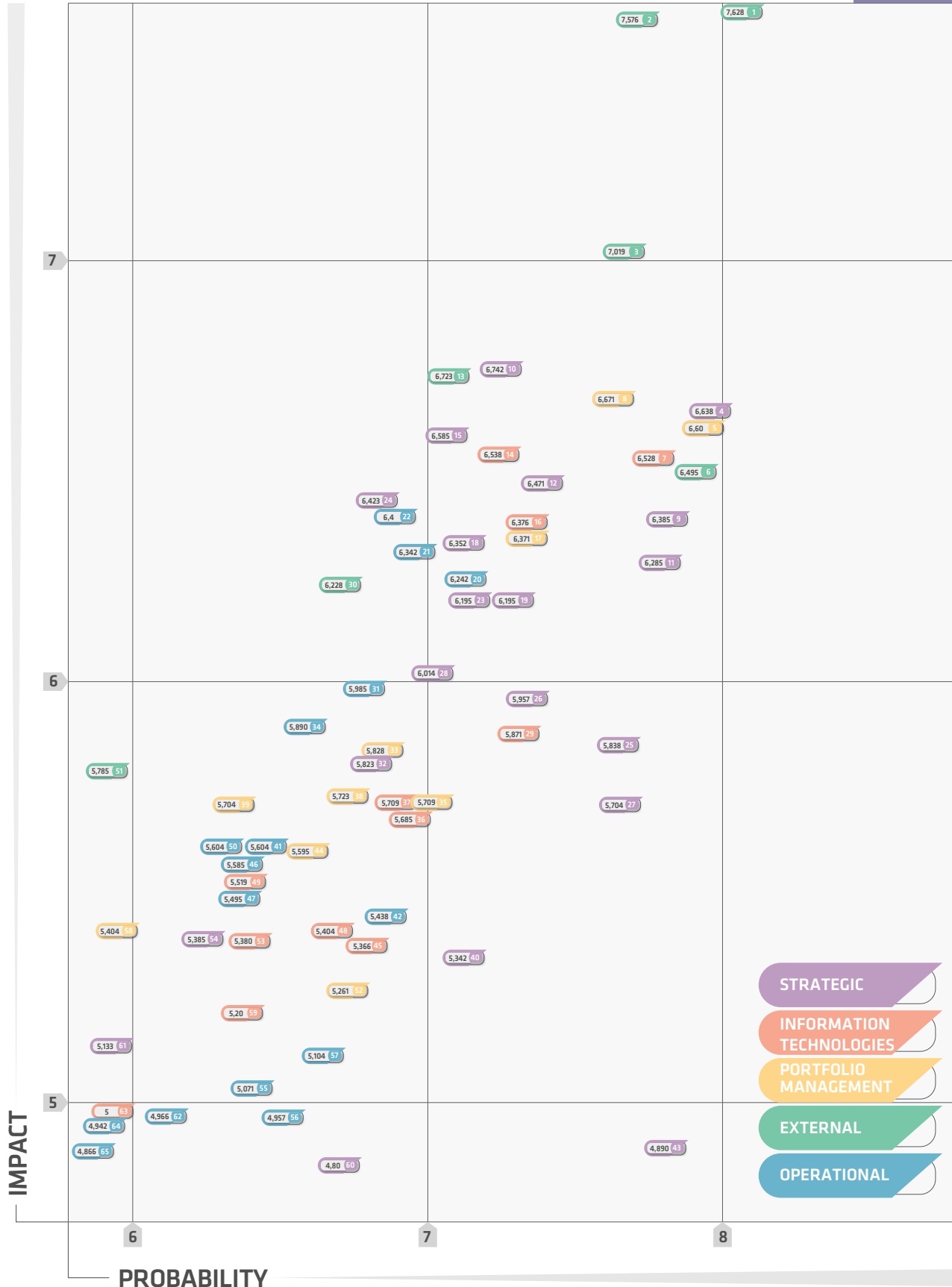
Appendix 1. Risk Map

2023



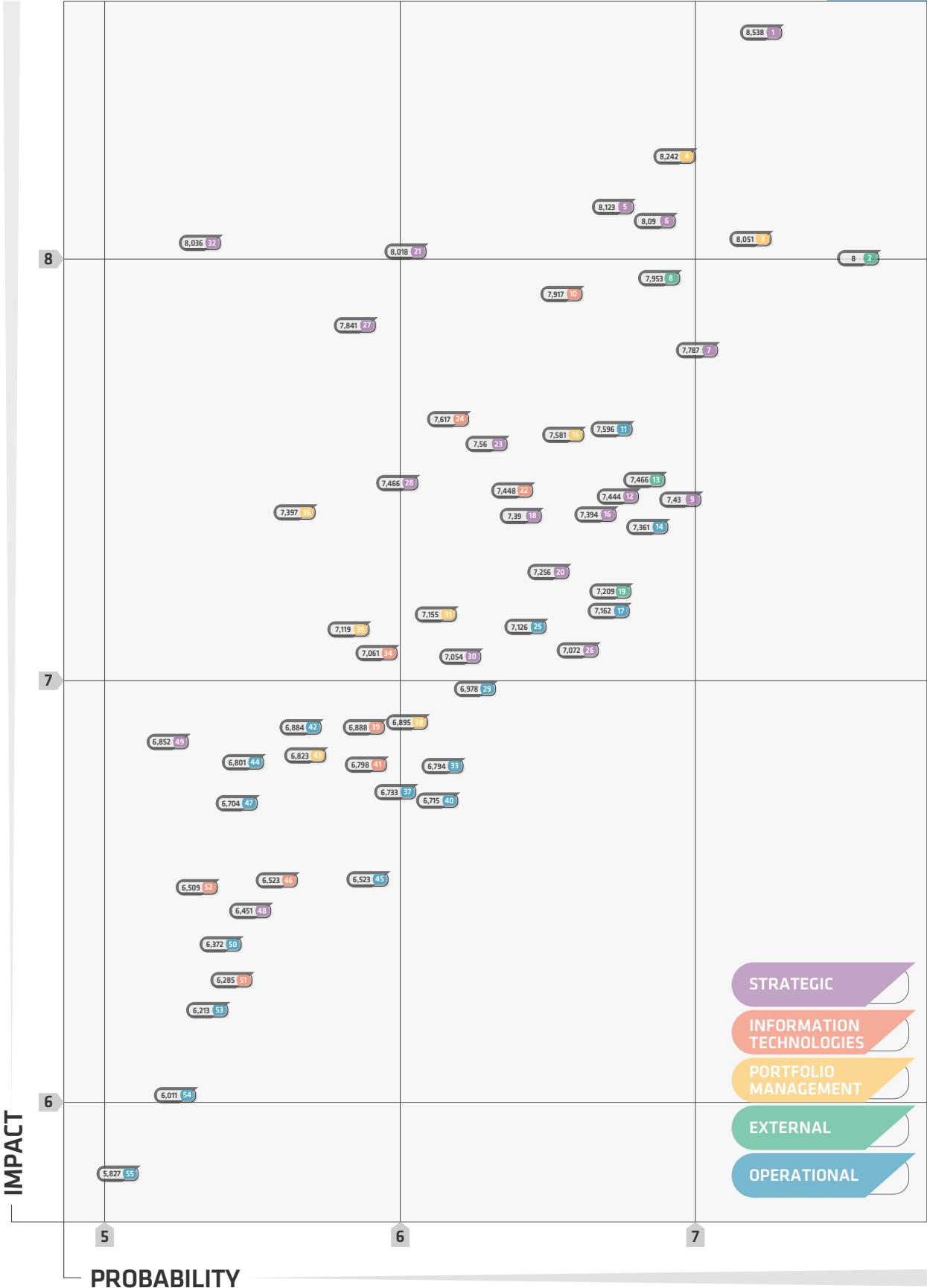
Appendix 1. Risk Map

2022



Appendix 1. Risk Map

2021



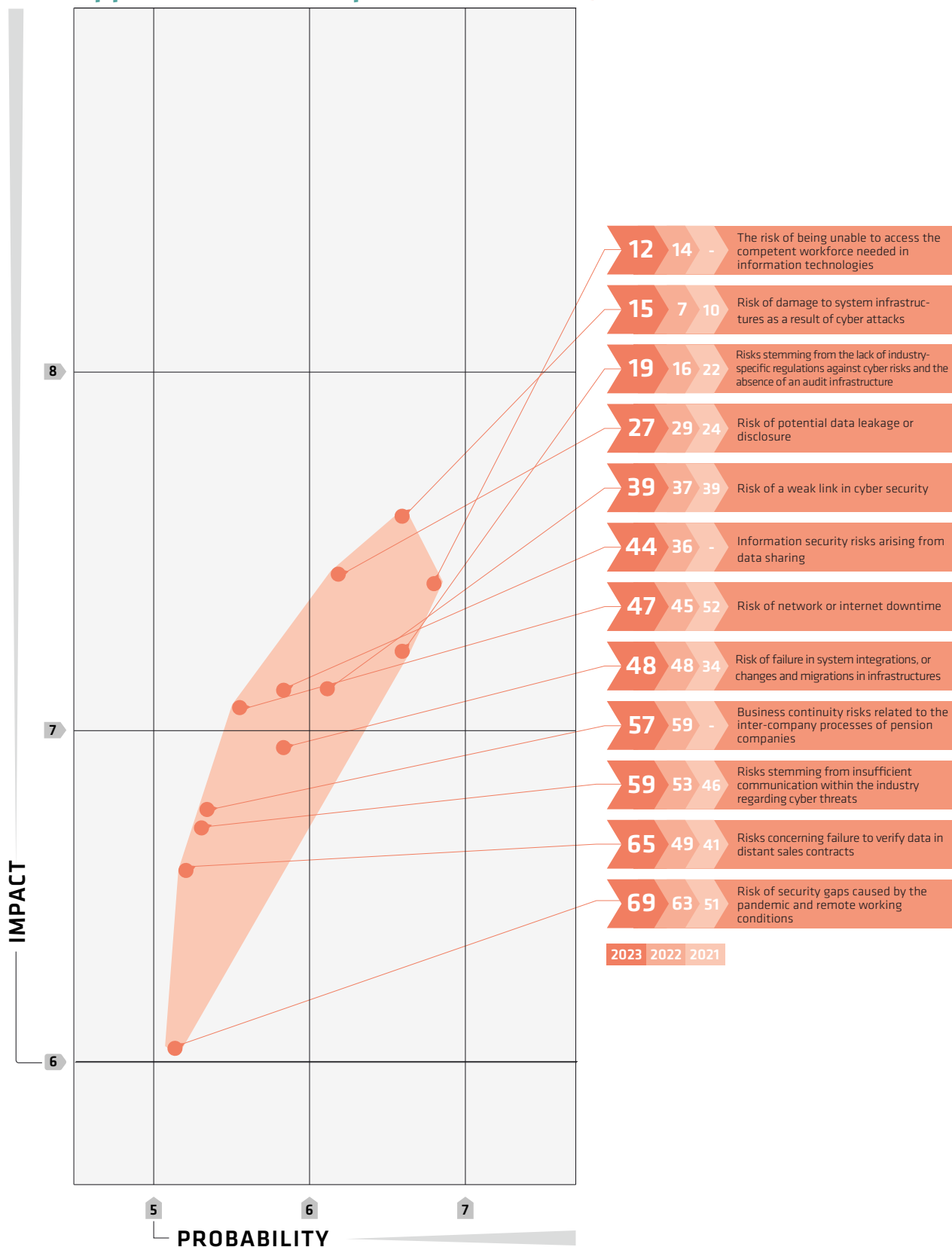
Appendix 1. Risk Map / Strategic Risks



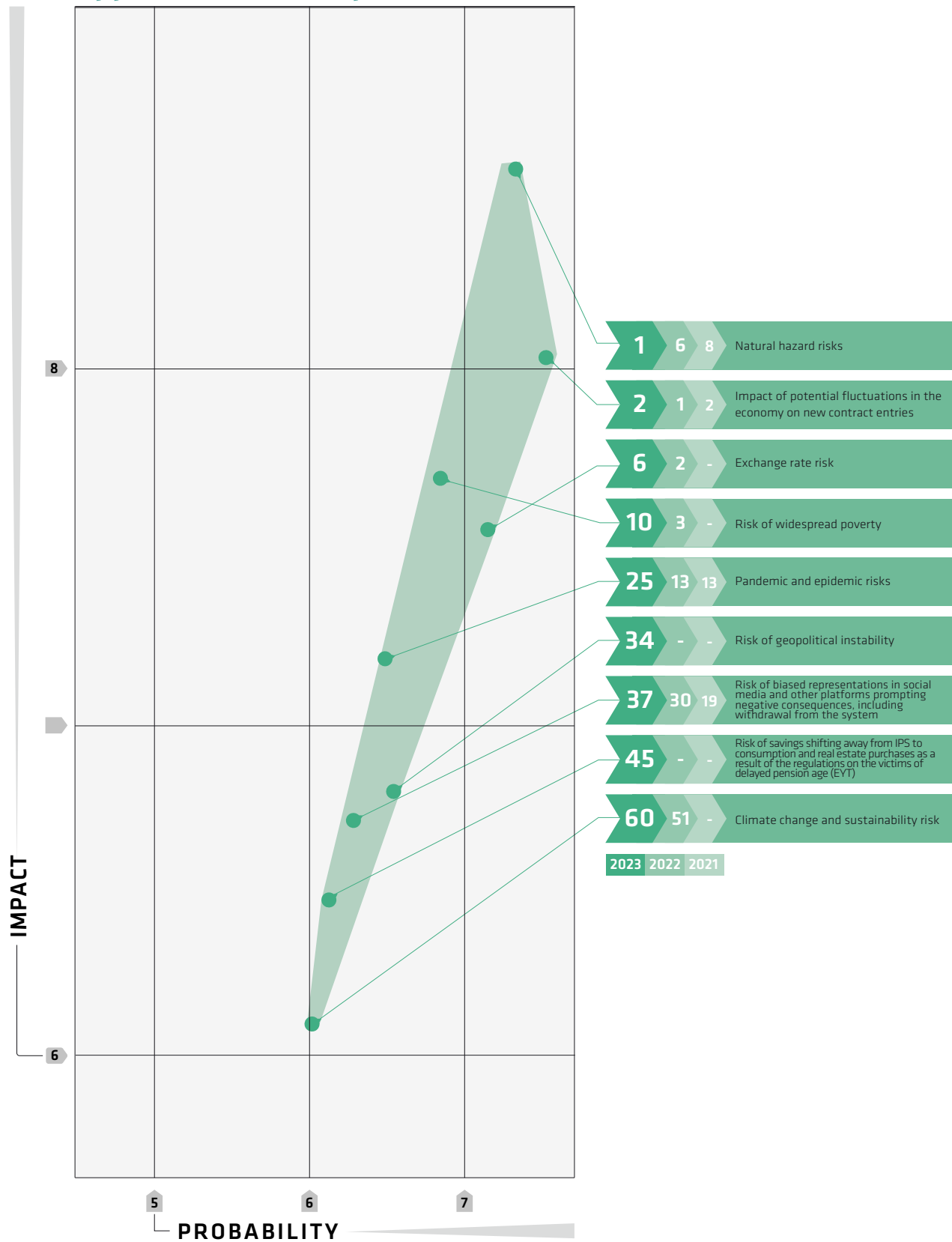
Appendix 1. Risk Map / Portfolio Management Risks



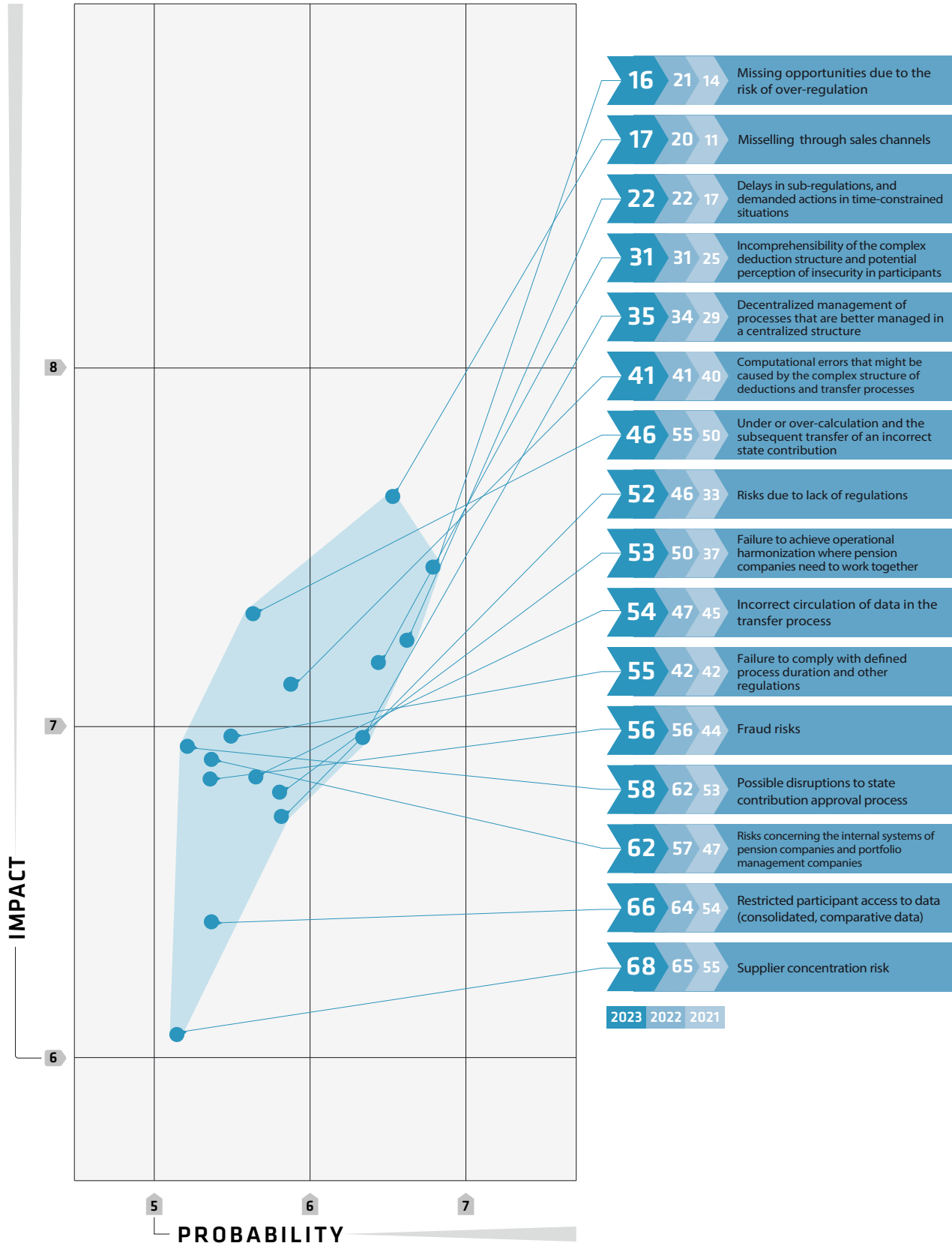
Appendix 1. Risk Map / Information Technologies Risks



Appendix 1. Risk Map / External Risks



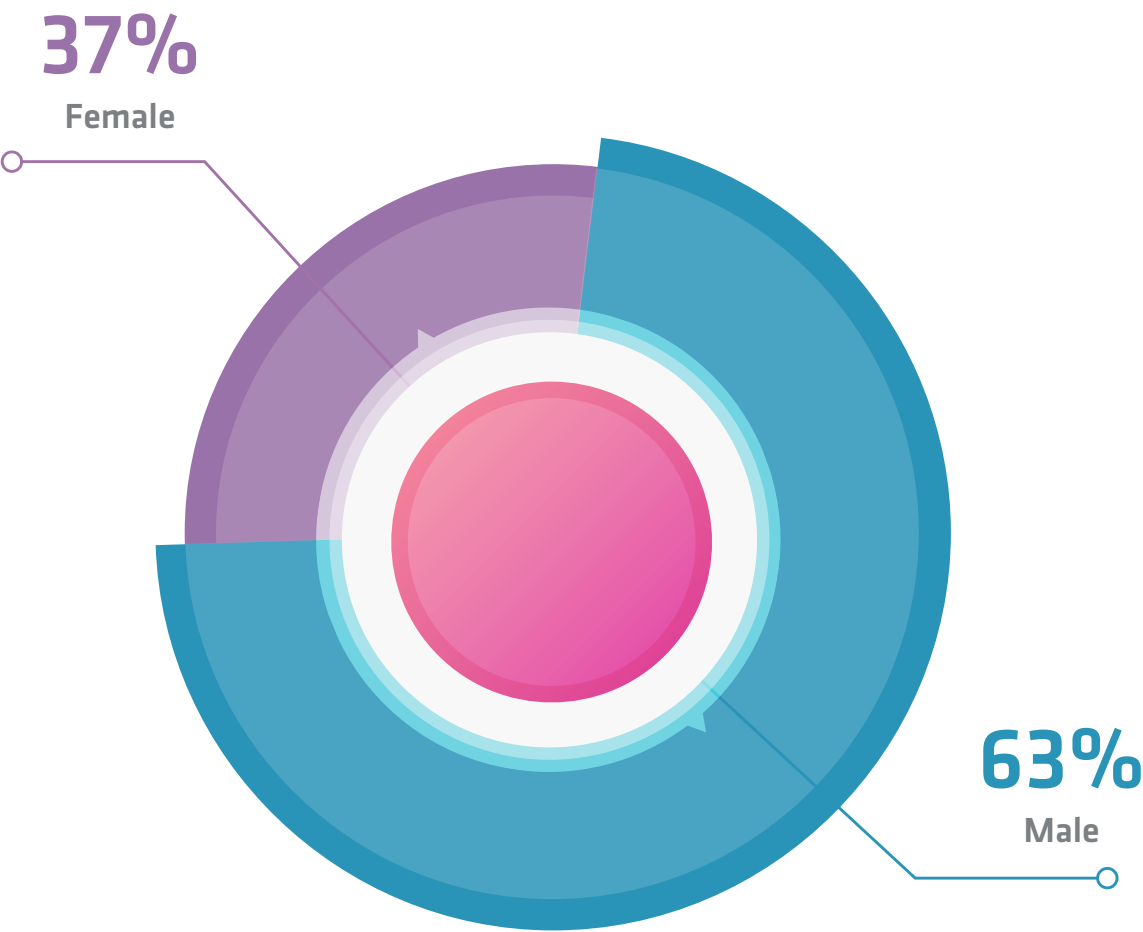
Appendix 1. Risk Map/ Operational Risks



Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Gender

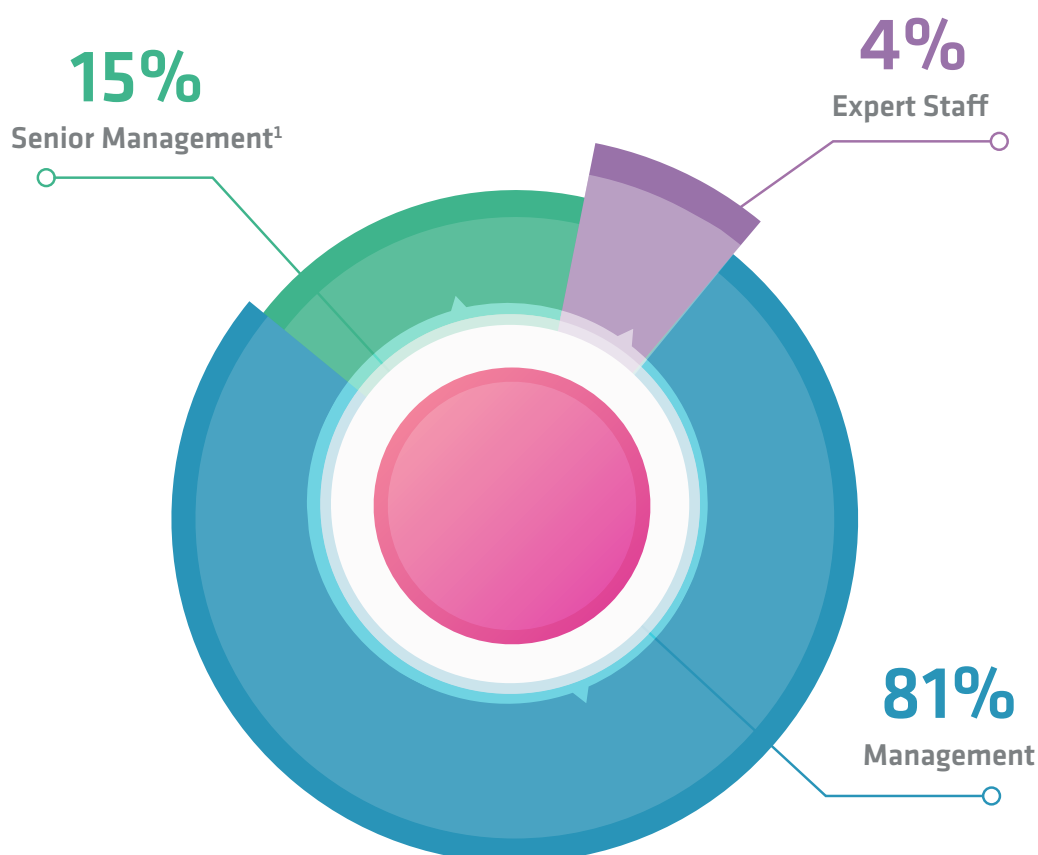
Of the 292 survey respondents, 109 are female and 183 are male.



Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Management Level

Of survey respondents, 81 percent are in management, while 15 percent are in senior management.

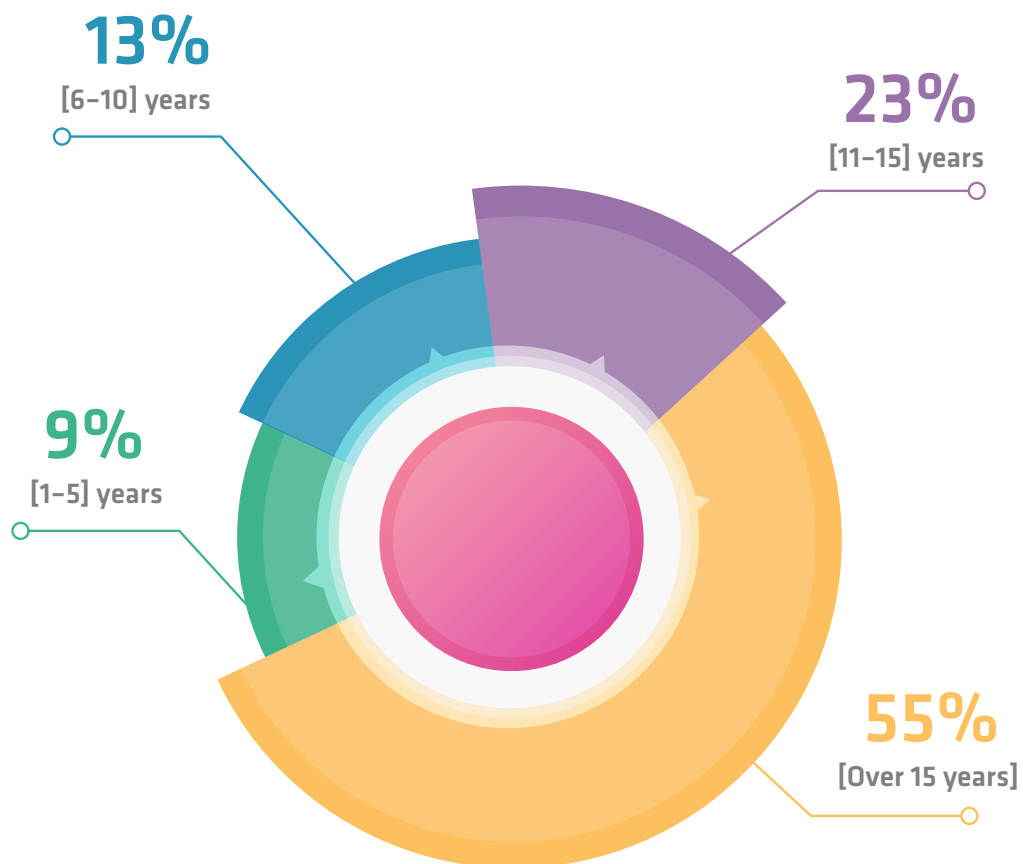


(1) Senior Management level refers to General Manager, CEO, CFO, CIO, CRO, Deputy General Manager, Director, Coordinator, Legal Consultancy, and senior management of the Regulatory and Supervisory Authority.

Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Industry Experience

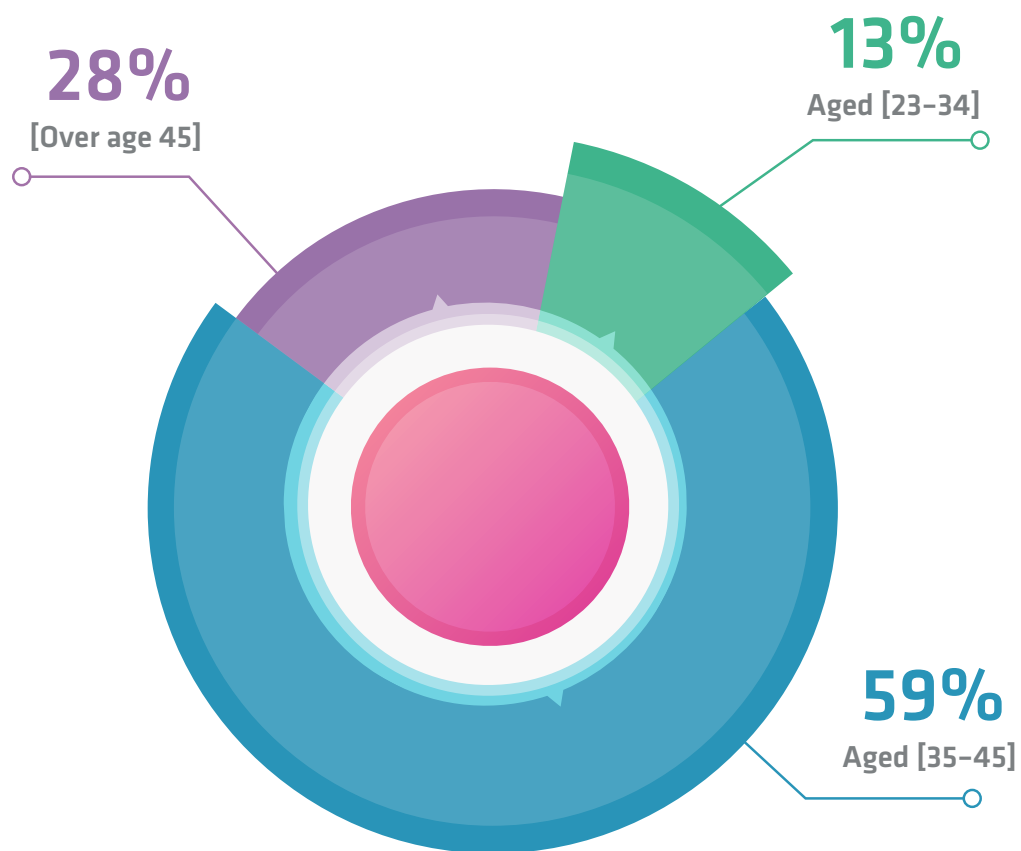
Of the survey respondents, 78 percent have over 11 years of industry experience.



Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Age

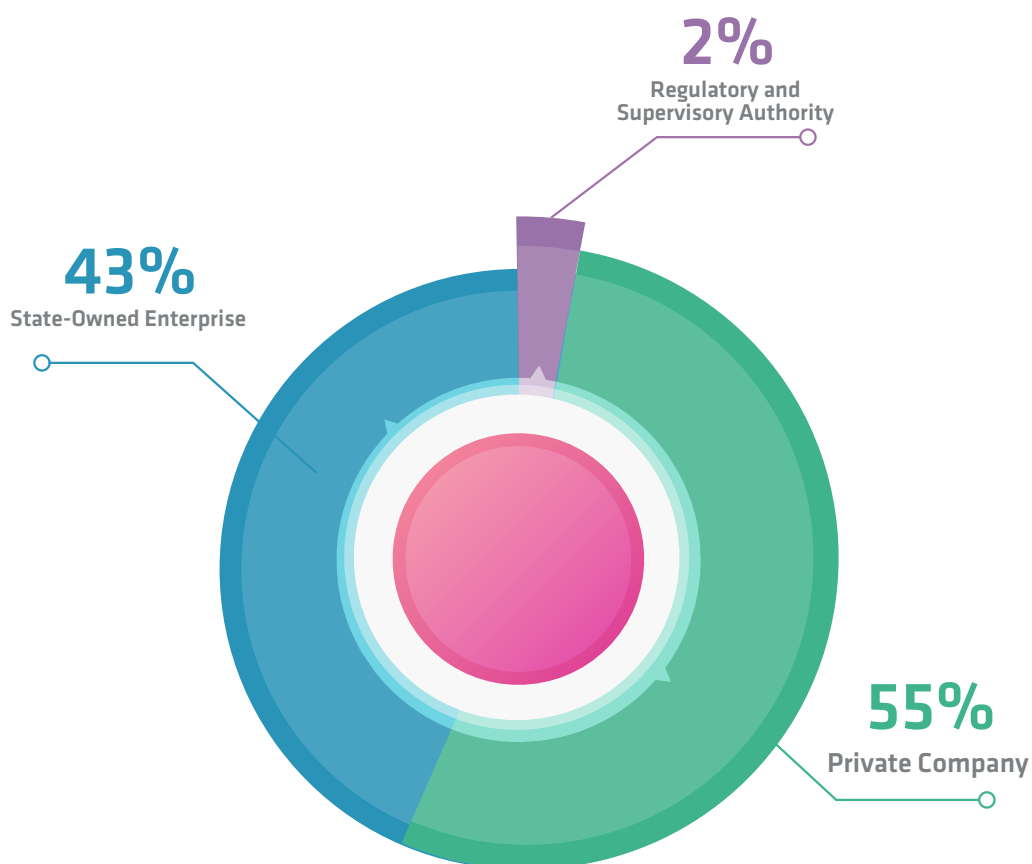
Of the survey participants, 87 percent are aged over 35.



Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Employment Institution

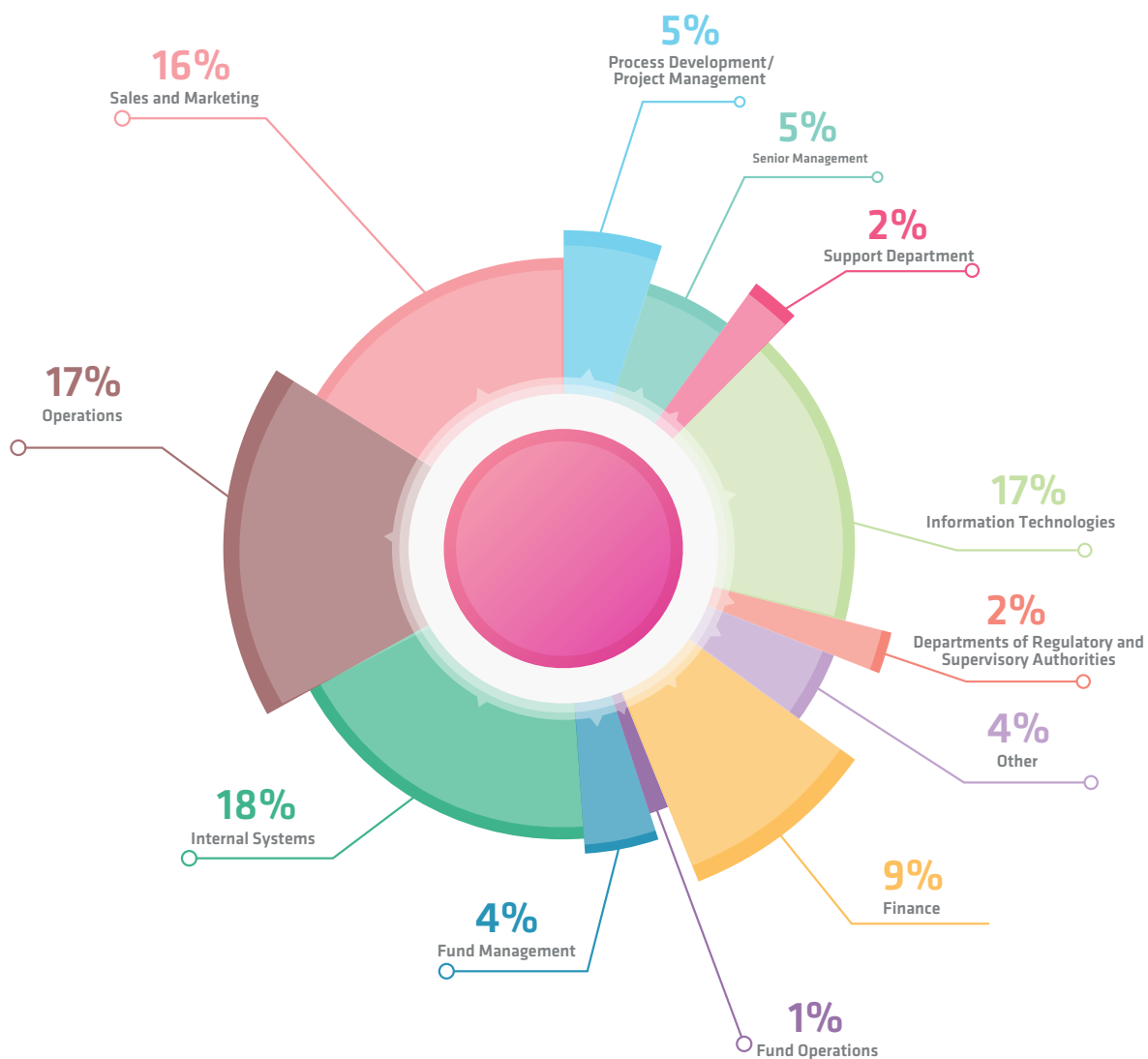
Of the survey respondents, 55 percent work for private companies, 43 percent work for state-owned enterprises, and 2 percent work for regulatory and supervisory authorities.



Appendix 2. Profile of Survey Respondents

Distribution of Survey Respondents By Work Department

Of the survey participants, 16 percent work in sales and marketing, 17 percent work in operations, 18 percent work in internal systems, and 17 percent work in information technologies department.



This report is the continuation of a series, the first of which was published in 2021.
You can learn more about the methodology by examining the first report available at
[https://egm.org.tr/Sites/1/upload/Şİes/Bireysel_Emeklilik_Sistemi_Risk_Envanteri -2021-1283.pdf](https://egm.org.tr/Sites/1/upload/Şİes/Bireysel_Emeklilik_Sistemi_Risk_Envanteri_-2021-1283.pdf) .

The Individual Pension System Risk Inventory was prepared and reviewed by the Internal Control and Risk Management and Internal Audit Departments of the Pension Monitoring Center based on survey results and was approved by the General Directorate.

Contact us at <https://egm.org.tr/bize-ulasin/bize-yazin/> for further inquiries or to leave suggestions concerning the report.

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August 2023