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WWZ research seminar

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Abstract

Title: Pension Fund's Illiquid Assets Allocation Under Liquidity and Capital Constraints

Abstract: This paper empirically assesses the impact of liquidity and capital constraints on the allocation of defined benefit pension funds to illiquid assets. Liquidity constraints result from short-term pension payments and collateral requirements on derivatives. Capital constraints follow from the requirement to retain sufficient capital to absorb unexpected losses. Liability duration and hedging affect the allocation to illiquid assets through both these constraints. First, we find a hump-shaped impact of liability duration on the illiquid assets allocation. Up to 17.5 years, liability duration positively affects the illiquid asset allocation. However, beyond this point the effect is reversed as the capital constraint dominates the liquidity constraint. Second, we find no evidence that interest rate hedging affects the illiquid assets allocation. Third, we do find that currency risk hedging positively impacts the illiquid assets allocation.