

Search for...



Welcome, ARTHUR (/login/my-account)






# LATINFINANCE

(/)

[Home \(/\)](#) / [2018 \(/magazine/2018\)](#) / [May / June 2018 \(/magazine/2018/may-june-2018\)](#) / Brazil's pension funds try to correct past mistakes

## Brazil's pension funds try to correct past mistakes

 ([http://twitter.com/intent/tweet?status=Brazil's pension funds try to correct past mistakes+http://www.latinfinance.com/magazine/2018/may-june-2018/brazils-pension-funds-try-to-correct-past-mistakes](http://twitter.com/intent/tweet?status=Brazil's+pension+funds+try+to+correct+past+mistakes+http://www.latinfinance.com/magazine/2018/may-june-2018/brazils-pension-funds-try-to-correct-past-mistakes))  ([http://www.linkedin.com/shareArticle?mini=true&url=http://www.latinfinance.com/magazine/2018/may-june-2018/brazils-pension-funds-try-to-correct-past-mistakes&title=Brazil's pension funds try to correct past mistakes&source=http://www.latinfinance.com](http://www.linkedin.com/shareArticle?mini=true&url=http://www.latinfinance.com/magazine/2018/may-june-2018/brazils-pension-funds-try-to-correct-past-mistakes&title=Brazil's+pension+funds+try+to+correct+past+mistakes&source=http://www.latinfinance.com))  (mailto:?Subject= Brazil's pension funds try to correct past mistakes &body=http://www.latinfinance.com/magazine/2018/may-june-2018/brazils-pension-funds-try-to-correct-past-mistakes)

[Save Story](#)

June 8, 2018 | **Rodrigo Amaral**

**Pension funds in Brazil are reeling from corruption scandals that caused billions of reais in losses. Now they are implementing stricter rules for picking investments, but options are slim.**

[Asset Management \(/topics/asset-management\)](#) [Bonds \(/topics/bonds\)](#) [Debt \(/topics/debt\)](#)

[Capital Markets \(/topics/capital-markets\)](#) [Corporate & Sovereign Strategy \(/topics/corporate-sovereign-strategy\)](#)

[Debenture \(/topics/debenture\)](#) [Economy & Policy \(/topics/economy-policy\)](#) [Equity \(/topics/equity\)](#)

[Fixed Income \(/topics/fixed-income\)](#) [Funds \(/topics/funds\)](#) [Project & Infrastructure Finance \(/topics/project-infrastructure-finance\)](#)

[Politics \(/topics/regulation/politics\)](#) [Special Reports \(/topics/in-depth/special-reports\)](#) [Features \(/topics/in-depth/features\)](#)

[Brazil \(/topics/regions/brazil\)](#)

With 842 billion reais (\$227 billion) in assets under management at the end of last year, Brazil's pension funds are a key source of funding for the local capital markets. But the industry's investment capacity has been severely compromised by years of poor performance and a series of high profile scandals.

The pension funds for employees of the state-owned postal service Correios, the state-owned banks Caixa Econômica Federal and Banco do Brasil, and the state-owned energy company Petrobras, among others, have amassed billions of reais of losses due to risky bets that were allegedly connected to fraud and kickback schemes.

The funds stand accused of diverting workers' contributions to companies that funneled money to politicians and political parties. Congress set up an investigation into the alleged irregularities in 2016, and the pension regulator Previc ordered the intervention of Postalis, another fund for post office workers, in October last year.

Now Brazil's top funds say they are determined to improve governance policies and strengthen internal controls so they can make better investments. But their efforts may stumble on a lack of options in the local capital markets, as investment returns shrink in an environment of record-low interest rates, and several

listed companies are still involved in corruption scandals.

"Sometimes investment managers argue that if you become too restrictive with the selection of assets, you will end up without options," says Gustavo Pimentel, managing director at Sitawi, a Rio de Janeiro-based consulting company that develops impact investing projects.

Brazil's pension funds posted a combined deficit of 36.1 billion reais last year, an improvement from the losses of 70.6 billion reais in 2016, Previc says. Not all the pension funds have underperformed: 141 out of 302 funds finished 2017 with a surplus, while 86 managed to balance their books. But 75 had losses, and several them are reeling from investments made in the past decade.

"Pension funds were taken over and used for reasons that diverged from their core mission, getting involved in corruption cases as a result," says Edivar Queiroz, CEO Luz Soluções Financeiras, a São Paulo-based asset manager.

### **Arrested executives**

Politicians have long used their clout over the state-owned companies that sponsor pension funds to appoint allies to their boards. Several managers, especially at the funds linked to state-owned firms, have been accused of working for their political bosses, rather than for pensioners.

The supposedly tainted funds include Previ at Banco do Brasil, which represents almost 22% of the industry, and Petros at Petrobras, which manages 10.4% of all pension assets in Brazil. Previ and Petros, along with Caixa's Funcef and Postalis, have come under investigation for alleged fraud through special vehicles created to invest in non-listed companies called FIPs.

Another federal investigation led to the arrest of several former executives at Postalis, which has an estimated deficit estimated of more than 6 billion reais.

The accused executives have denied any wrongdoings, but the investigations have laid bare the poor governance structures in the industry. "It is hard to believe, but until recently, the function of the risk manager practically did not exist in pension funds," Queiroz says.

Some companies that received large amounts of pension fund investments through FIPs suffered large losses after they became targets of corruption investigations. For example, a group of funds are reportedly seeking 8 billion reais in compensation for the losses they accrued from their holdings in Sete Brasil, an oil rig company caught up in the corruption investigations at Petrobras. Now pressure is piling up on fund managers to do a better job making investments, and ethics have risen to top of the list of criteria to be considered.

"The facts have shown that assets that were targets of court cases or were involved in corruption investigations delivered significant negative financial results," Petros President Walter Mendes says. "Stricter ethics criteria and anti-corruption procedures mitigate investment risks, with a positive impact on pricing."

In September 2017, Petros said it would levy additional charges on contributors for the next 18 years to cover 27.7 billion reais in losses, partly due to bad investments. Those investments include an 8.53% stake in Eldorado, a pulp and paper company once owned by J&F Investimentos, the group that also controls the meatpacker JBS. Wesley Batista, the former CEO of JBS, and his brother, Joesley Batista, the former chairman, were arrested on suspicion of paying bribes to more than 1,800 politicians.

But now Petros says it is working to improve its governance policies and its methods for picking investments. The fund says that it has set up a compliance program, strengthened internal controls and audit structures,

and established new directives for hiring of board members. It also says it is updating the selection process for investments, including an emphasis on environment, social and governance criteria.

"Among the measures adopted, Petros is now performing reputation analyses and background checks on those who are appointed as board members at companies where we invest and at all service providers," Mendes says.

### **Accelerating efforts**

In Previc's latest action plan, the regulator said "atypical" operations had threatened the credibility of Brazil's pension fund industry in recent years and it vowed to implement measures to repair the damage. Previc promised to review of the role that independent auditors play at pension funds and modernize governance structures, with a tighter focus on 17 funds that are of "systemic relevance" — a group that includes Previ, Petros, Funcef and Postalis.

At some funds, the process is already well under way. Fundação Ceres, which manages the pension plans of workers at eight state-owned agricultural research and development companies, started to strengthen its corporate governance structures back in 2010, according to Dante Scolari, the head of investments.

"We evaluate proposals from a business perspective, but also according to other criteria. Everyone who does business with Fundação Ceres needs to follow our code of ethics," Scolari says.

Any hint that a company may be dodging the rules is enough to get it scratched from Ceres' portfolio.

"We do not trade with any entity that has an image problem, that is being mentioned in a negative light by the media. It has happened even with big asset managers that have a lot of weight in the market, and we have avoided doing business with international banks for that reason," he says.

Advocates for better corporate governance in Brazil hope this kind of approach among institutional investors will lead to better practices in the economy as a whole. And the anticorruption law, passed in 2013, carries a real threat of significant financial losses for companies that do not shape up, according to Pimentel.

"Investors have become much more aware of this subject," he says. "Some funds have gotten to a point where they veto investments or reduce their shares in companies that have been merely accused of malfeasance. Previously, they would have waited a final verdict from the courts before taking such a step."

### **New attitudes**

Mauro Cunha, CEO of the capital markets investors association Amec, says recent actions reveal that institutional investors have a new attitude.

In one example, pension funds helped force a change of leadership at BRF, a poultry producer accused of paying bribes to avoid sanitary inspections at processing plants. In another example, several pension funds, including Petros, Previ and Funcef, have joined a lawsuit against Petrobras, with minority shareholders seeking compensation for losses from the company's participation in bribery schemes.

But the good intentions are coming up against the lack of choices in Brazil's securities markets, which still offer limited options to investors, especially those who want to focus on ESG factors.

The list of Brazilian companies accused of corruption includes Petrobras, Odebrecht, Banco do Brasil, Caixa, JBS, BRF, Andrade Gutierrez, Bradesco and many others — a veritable who's who of blue chip bond issuers

that would be excluded from a strictly compliant ESG portfolio.

Many Brazilian companies may not view compliance and good governance as vital aspects of doing business, but to change the situation, Cunha says regulators and investors need to hit CEOs where it counts — in their pockets.

"If regulators and investors do not fully commit to the vision that corruption and ethics are relevant factors from an investment point of view, progress will remain slow," he says.

Cunha acknowledges that some progress has been made. Brazil's securities regulator CVM, for example, has demanded more transparency from companies that want to raise funds in the capital markets. "Regulation has evolved. Governance themes have become much more relevant in CVM's rules on reference documents," he says.

"There is much more information that is useful for investors to distinguish companies that do their homework from those that merely ask a lawyer to fill in the forms for them."

Brazil's pension funds can devote up to 10% of their investment portfolios to foreign markets, and Previc has recently announced measures that make it easier to allocate money abroad. So institutional investors can always look elsewhere if they do not find adequate investment opportunities at home, Cunha says.

"There is no need to invest in Brazil. If there are no adequate assets in the market, investors can diversify abroad," he says. **LF**

## Related Stories

---

- > [EcoEnterprises earns commitments on third fund \(/daily-briefs/2018/6/11/ecoenterprises-earns-commitments-on-third-fund\)](/daily-briefs/2018/6/11/ecoenterprises-earns-commitments-on-third-fund)
- > [Movida moves local bonds \(/daily-briefs/2018/6/11/movida-moves-local-bonds\)](/daily-briefs/2018/6/11/movida-moves-local-bonds)
- > [CAF ponders Sterling return \(/daily-briefs/2018/6/11/caf-ponders-sterling-return\)](/daily-briefs/2018/6/11/caf-ponders-sterling-return)
- > [Colombia inches toward Basel III \(/daily-briefs/2018/6/11/colombia-inches-toward-basel-iii\)](/daily-briefs/2018/6/11/colombia-inches-toward-basel-iii)
- > [Barbados bondholders await clarity amid slide \(/daily-briefs/2018/6/11/barbados-bondholders-await-clarity-amid-slide\)](/daily-briefs/2018/6/11/barbados-bondholders-await-clarity-amid-slide)

---

All material is subject to strictly enforced copyright terms & conditions and cannot be repurposed or reproduced. © 2018 Latin American Financial Publications Inc.