

Pension saving: Local funding for local development

Last week we asked whether pension fund saving should be considered a source of funding for national development. While governments might be tempted to use local sources to meet their financial needs, this is not good long-term strategy. The price of forcing citizen saving into government funding is higher interest rates, lower confidence and potentially economic disaster. Still, developing country pension funds may be key to local economic development.¹

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Global development requires funding. The OECD estimates a shortfall of some \$4 trillion in such funding. Much of the capital is held in developed countries. These sources are typically unreliable when needed most. Experience has shown that, during crises, portfolio flows to developing countries often drop off quickly as they are re-diverted to urgent needs in source countries. This is where local sources come in. Pension assets in emerging markets amount to some \$2 trillion.

Long-term fit

Pension arrangements are a good match for development investment because they have a long-term perspective. A large proportion of member contributions made today, especially into defined benefit schemes, will not be needed as benefits for many decades. This puts them in the ideal position to apply assets to local projects likely to deliver returns in the long run, such as energy infrastructure or housing projects, even rail.

Local knowledge, local stakeholders

In-country pension funds also have a better sense of the priorities of that country. This does not mean that their allocation to projects should be politically influenced. Far from it. They are able to distinguish between *want* and *need*, allocating money on the lines of sound priorities.

These funds not only have a sound understanding of such need. Their stakeholders benefit from their actions. Effective infrastructure benefits their members and beneficiaries. This may be direct, in the form of more reliable energy, say, or cheaper costs of transporting goods. Such investment typically also stimulates the economy, generating indirect benefits in the form of better returns across a range of other investment activities.

Such activity is helpful not only to the performance of the fund and the country. It also typically stimulates other improvements in fund governance and operations. It also often leads to a more effective regulatory framework governing that fund and its peers because it



demonstrates the possibilities unleashed by good governance and sound decision-making.

Several examples

It is hard to believe that the much-lauded Canadian pension fund giants had humble beginnings. The mighty Ontario Teachers' Pension Plan was wholly invested in government bonds in the 1980s. Only in the 2000s did it diversify into infrastructure and natural resources, becoming a world leader in the process.

Malaysia's Employees Provident Fund, with assets of more than \$200b, is an excellent example of local development and sound governance in a developing country. And our own Government Employees Pension Fund, soundly watched by an independent press, has pressed on with excellent local development initiatives.

Pension fund trustees tend to be fixated with local problems. This often encourages offshore diversification. Yet they have the unique opportunity to invest at good returns to address many of these local challenges. **Rob Rusconi**

¹ Key source: Davis, R, R Rusconi & A Levine (2024), 'How to Harness local Investors in Emerging Markets: The Example of Local Pension Funds', *Equitable Growth, Finance and Institutions Insight*, World Bank