The Mansion House papers

Background and trustee perspective

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What is the “problem”/opportunity?

£1.5trn

DB pension schemes, and the PPF, are better funded than ever

UK private sector defined benefit (DB) pension schemes hold around **£1.5 trillion** in assets and the majority are now in surplus on a ‘low dependency’ basis

DB schemes have significantly de-risked

The proportion of DB scheme assets invested in equities fell from **61%** in 2006 to **20%** in 2022. As a result, future investment returns are expected to be low, and be further impacted by proposed changes to the funding regulations.

Belief: If UK schemes invest more in higher growth assets it would benefit employers, DB and DC members and the UK economy.

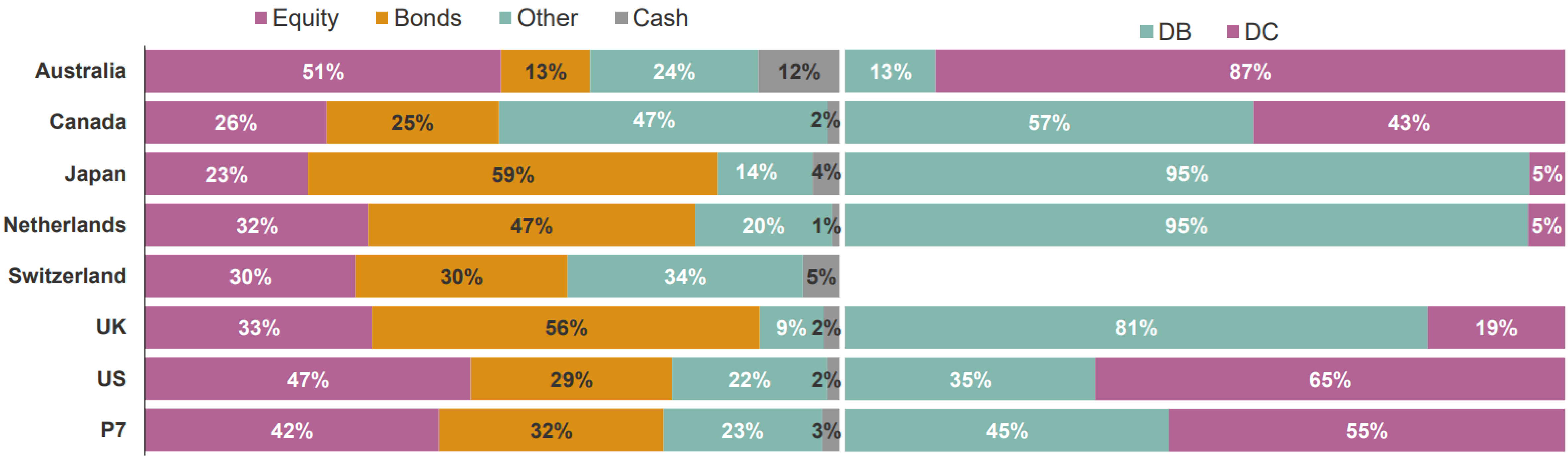
Using the capital of DB schemes more productively could generate **billions of pounds** of additional returns each year to benefit these stakeholders.

Belief: Consolidation will improve investment, governance, efficiency and outcomes

DC consolidation has been a success. Many see consolidation in the DB market as highly desirable and believe it will result in higher allocations to productive assets

How are pensions invested in the UK and internationally?

- The UK is one of the largest seven markets by its pension assets. The others are shown in the chart below.
- Across all pension investments, there is a clear sign of a reduced home bias in equities over the past 20-year period, with the weight having fallen on average from 67% in 2002 to 38% in 2022. The UK has remained broadly in the middle of the pack for domestic equity exposure when considered as a proportion of its total equity exposure.
- Additionally, the UK has a 33% exposure to equities across all pension investments, which puts it in third place compared with the other six countries.



https://www.thinkingaheadinstitute.org/research-papers/global-pension-assets-study-2023/

What are the concerns for trustees?

Security of benefits

Trustees primarily want to ensure benefits are paid in full as they fall due. At the very least, any changes should not lower the probability that members will receive their benefits in full.

Upside benefits

Trustee would be more willing to take (modest) additional risk if the benefits of any surplus were shared with the members eg through discretionary increases or one off lump sums

Downside protection

Trustees may be more willing to take additional risk if the downside was mitigated eg through:

- Surplus in the scheme
- High quality contingent assets
- Other benefit guarantees (PPF?)
- Employer ability to make good any future shortfall

Ultimately, will Trustees want to take additional risk?

Trustees are not concerned with broader economic benefits and interests of other groups (such as DC members)

Any decisions will be very scheme specific, and depend on employer covenant, upside benefits and downside protection.

What are some of the practical consolidation challenges?

- Should the sponsor link be severed? Is this in member interests?
- Bandwidth of trustees and sponsors to consider merits and make decisions
- Administration onboarding benefit designs and operation of discretions
- Transitioning investments and enormous trading volumes
- Consolidator resourcing to process highly complex onboarding and ongoing administration
- Data cleaning, rectifications and GMP equalisation
- Costs of support from advisors and suppliers and associated resource implications