Annual Funding Statement 2015

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ACA Sessional Meeting

Thursday 25 June 2015

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Outline

1. Financial conditions and implications for scheme funding
2. Managing risks and increases in deficits
3. What you can expect from us
4. Further guidance
5. Questions and discussion

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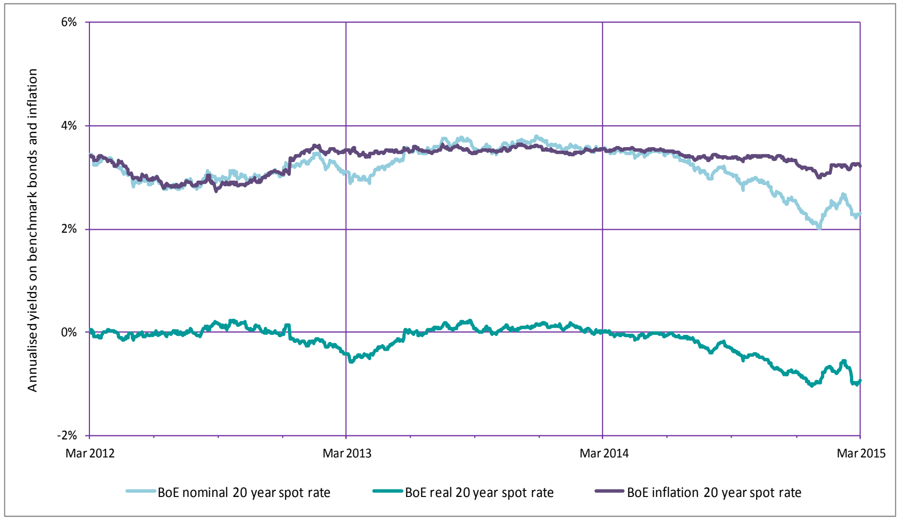
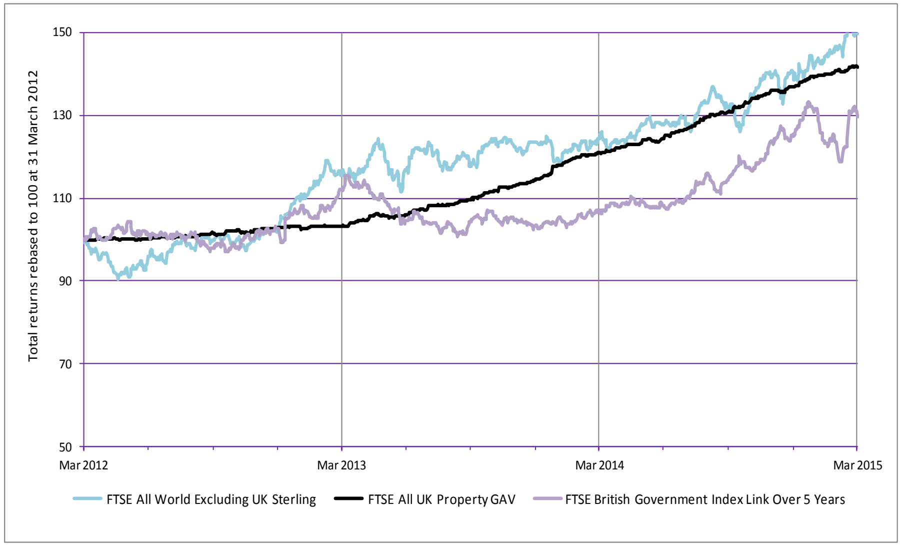
Financial conditions: past three years





- Reduced nominal and real yields
- Good investment returns
- But ....

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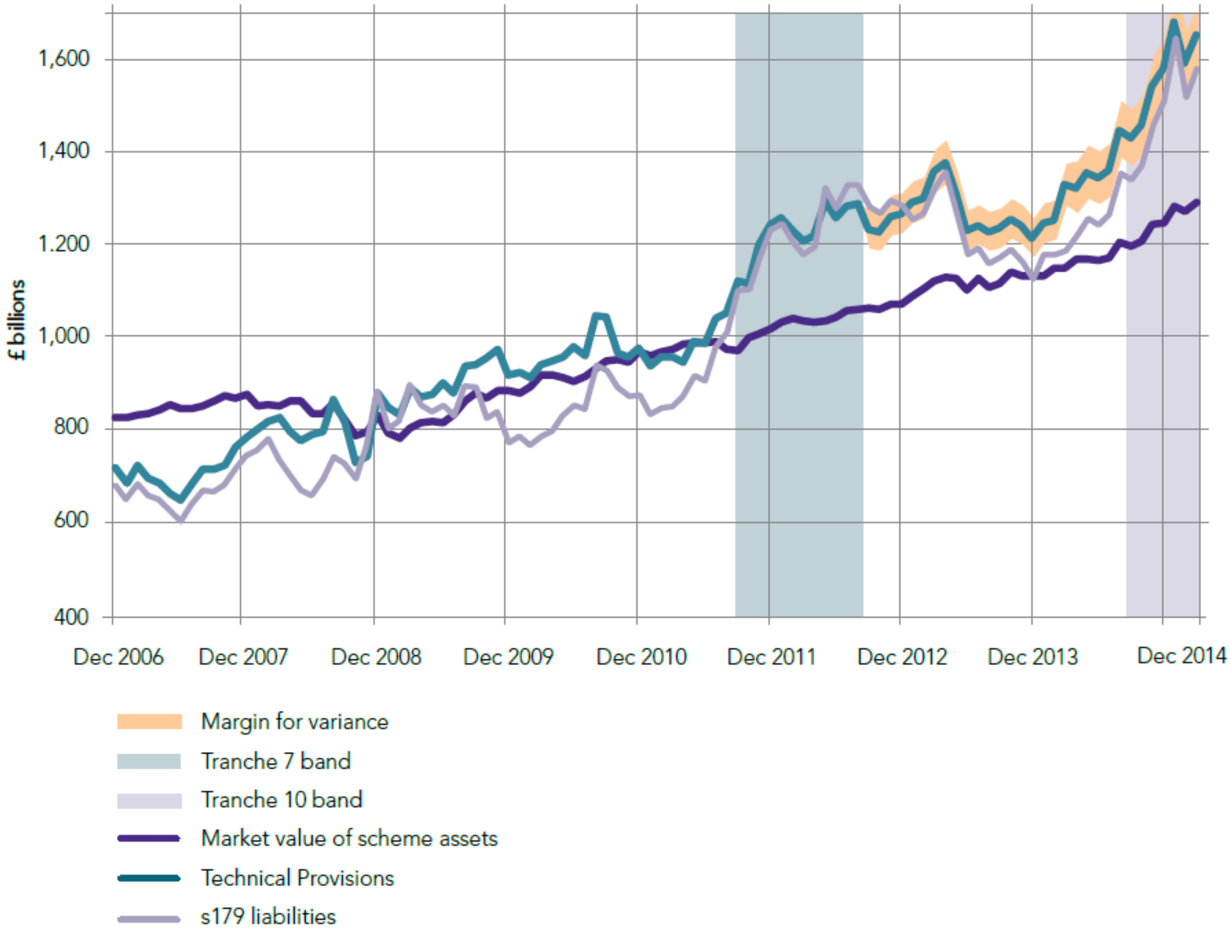
Estimated asset-liability positions
(all DB schemes)



Source(s): The Pension Protection Fund (PPF), The Pensions Regulator

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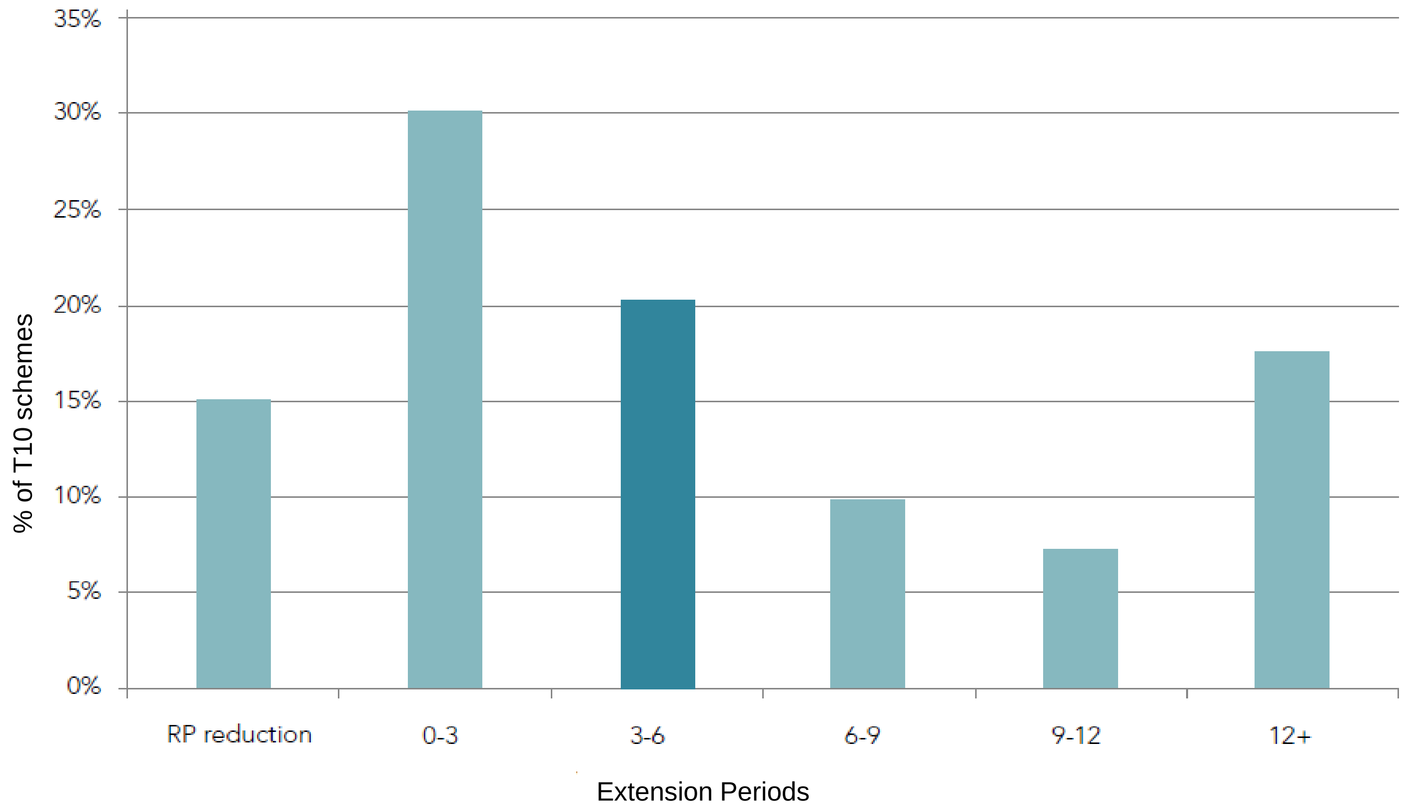
Financial conditions: future outlook

- Outlook for future investment returns
  - Considerable uncertainty about future economic and financial conditions
  - Market expectations: interest rates to remain lower for longer, and to revert to lower long-term levels.

- Most funding strategies likely to be based on lower expected investment returns.

- But a scheme specific assessment

Impact on recovery periods
(if contributions maintained)



Source: The Pensions Regulator

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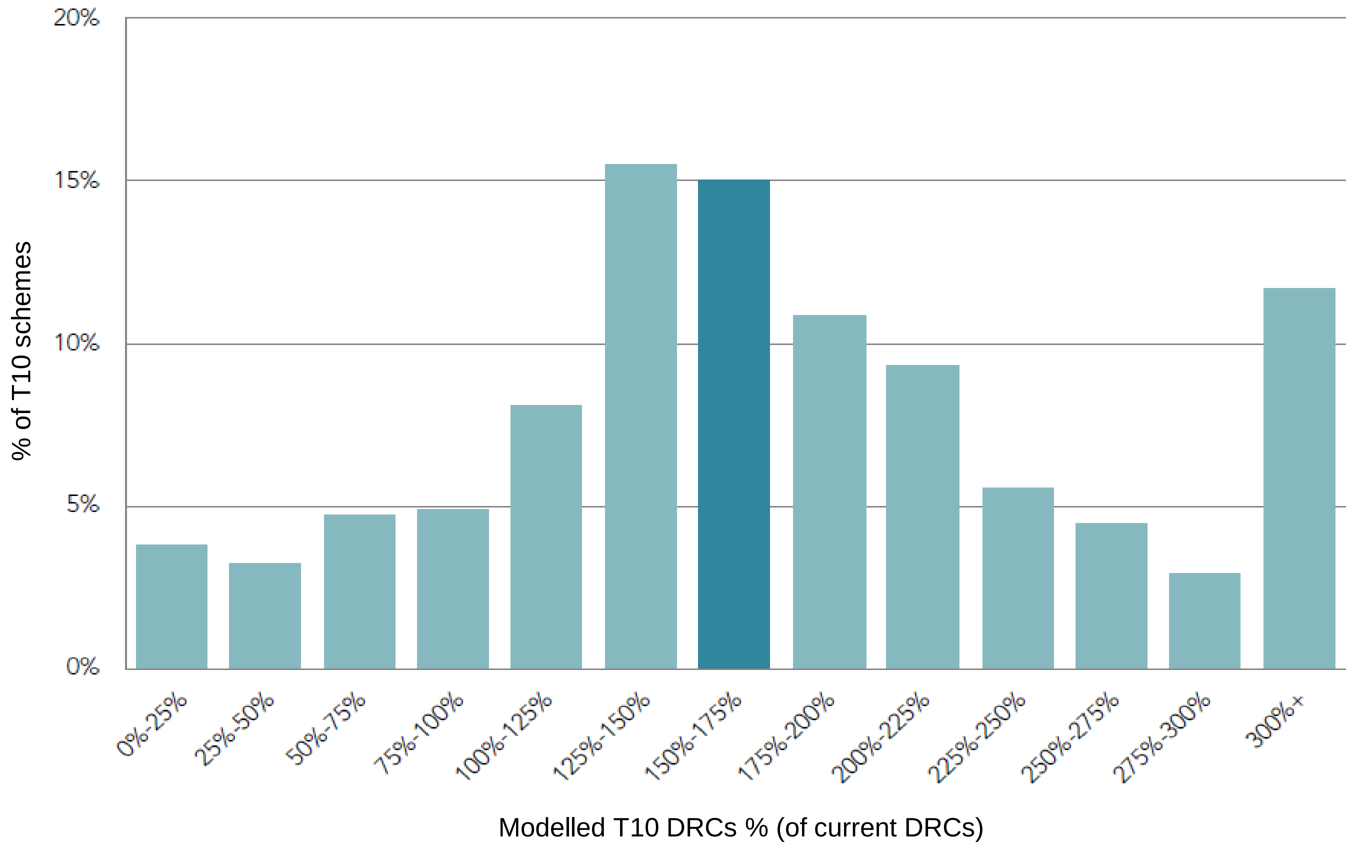
Impact on contributions
(if recovery plan end dates maintained)



Source: The Pensions Regulator

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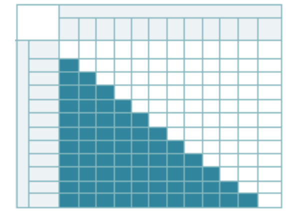
Impact on contributions
(relative to sponsor's profit)

Current DRCs as % of 2011 PBT	Modelled T10 DRCs as % of latest PBT											
	0	0–10%	10–20%	20–30%	30–40%	40–50%	50–60%	60–70%	70–80%	80–90%	90–100%	100% +
0	11	27	2	2	0	1	1	0	0	0	2	4
0–10%	24	163	54	21	11	4	3	4	2	1	0	4
10–20%	12	22	32	24	23	10	7	1	2	1	0	10
20–30%	5	7	13	20	12	11	7	8	4	2	2	8
30–40%	3	5	7	9	8	7	10	1	4	1	4	11
40–50%	3	3	1	2	3	3	1	5	4	2	2	18
50-60%	0	2	2	2	3	2	2	6	3	3	5	10
60–70%	2	1	1	1	0	0	3	5	2	3	0	9
70–80%	3	1	2	3	2	2	2	4	3	2	1	11
80–90%	0	0	2	0	0	1	1	2	1	2	0	13
90–100%	0	1	0	1	0	2	0	1	0	0	1	11
100%+	10	2	2	3	5	7	5	7	5	3	4	81

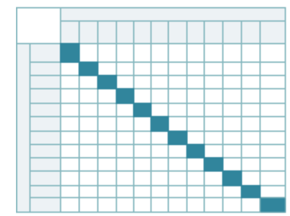
Source(s): The Pensions Regulator, Financial Analysis Made Easy published by Bureau van Dijk

Group A



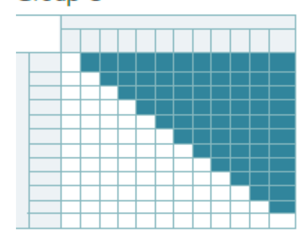
A –T10 DRCs/PBT < T7

Group B



B –T10 DRCs/PBT ~ T7

Group C



C –T10 DRCs/PBT > T7

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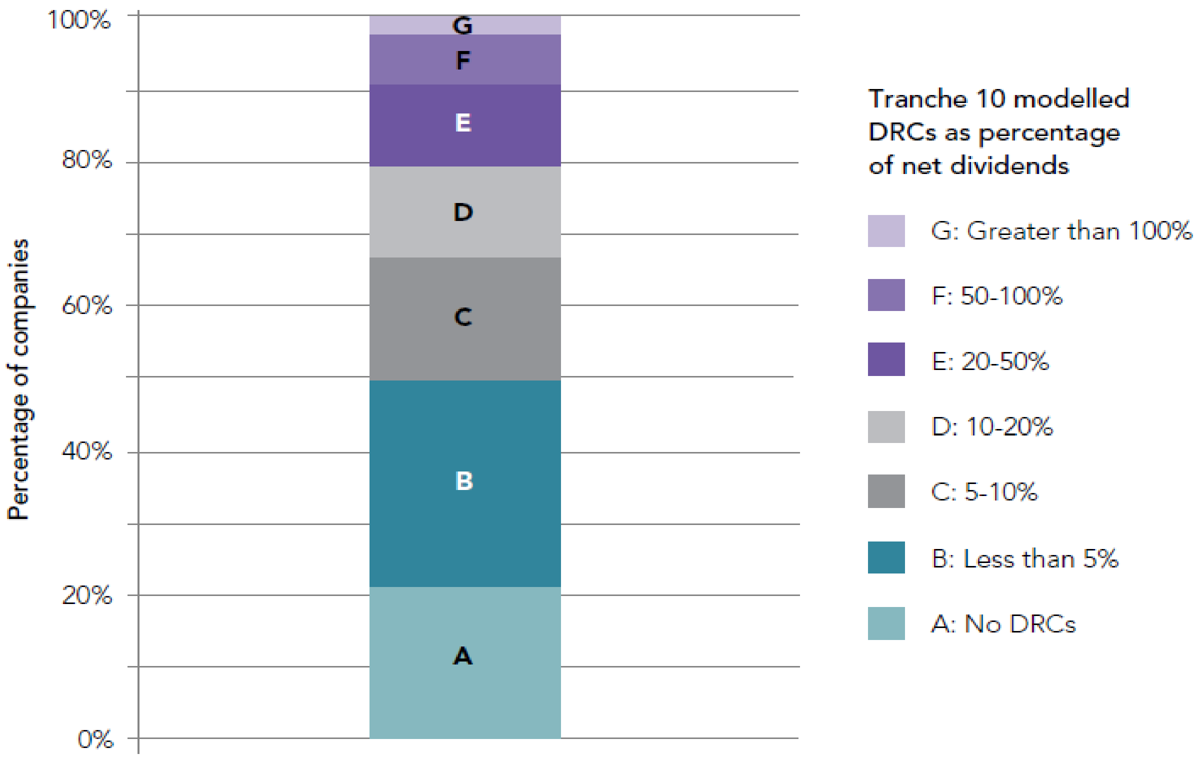
Impact on contributions
(relative to dividends – FTSE 350 companies only)



Source(s): The Pensions Regulator, Capita Registrars and Financial Analysis Made Easy published by Bureau van Dijk

Summary

- Bigger deficits
- Manageable for most schemes
- But challenges for some

Managing risk in uncertain markets

- Code: Need to manage risks in funding, investment and covenant in an integrated manner.
- Code: Understand the ability for employer to address a range of likely adverse outcomes.

- Where schemes experiences are less favourable than assumptions, consider contingency plans and take action.
- Assuming gilt reversion in 2015 valuations: consider the impact of assumptions not being borne out (including past) - scenario and contingency planning.

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Affordability: Managing increased deficits

- Flexibility in the regime to set funding strategies tailored to scheme and employer circumstances.
- Use of flexibilities should be based on specific circumstances and risk profile.
- Schemes with capacity to take additional risk – modest increases in DRCs, modest RP extensions and/or changing assumptions relating to investment returns.
- Schemes with more limited capacity to take additional risk – higher DRCs with a view to maintaining the same recovery plan end date.

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Balancing needs of scheme and employer

- Code: Trustees and employers should work collaboratively
- Code: Appropriate funding outcome recognises both scheme and employer needs

- Where affordability is constrained (including sustainable growth) trustees will need a higher level of due diligence:
  - Understand
  - Mitigate
  - Monitor

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What you can expect from us

- Risk indicators reviewed annually to reflect economic and market conditions
- Proactive engagement continues
- Engagement with schemes: focus on trustees' quality of decision making and contingency planning
- Further guidance to support the code

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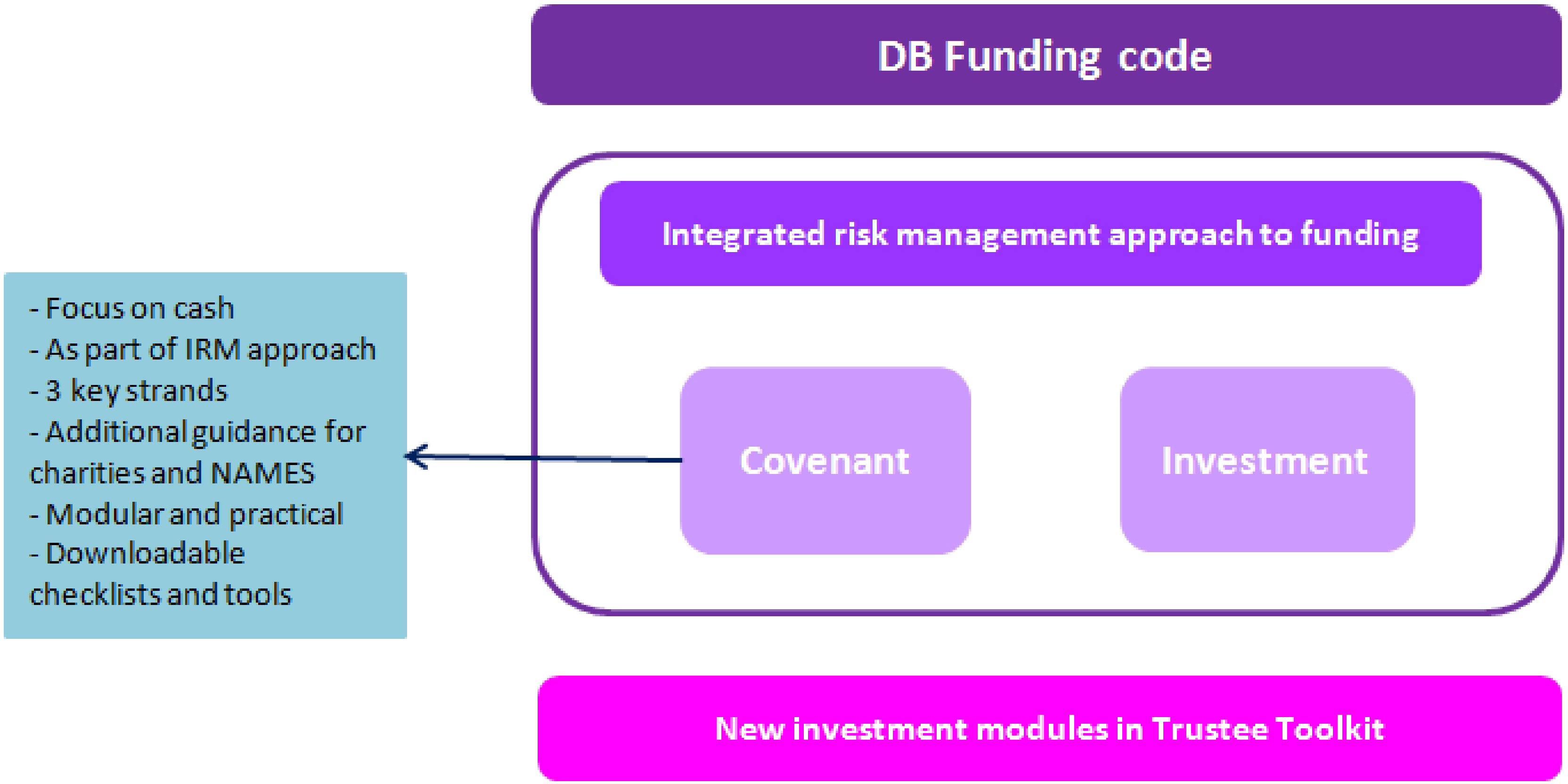
Forthcoming DB guidance



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Key points

- Challenging market conditions meaning larger deficits
- Anticipate lower expected investment returns
- Most schemes will be able to manage deficits
- Use of flexibilities should be based on specific circumstances and risk profile
- Higher due diligence required where affordability is constrained
- When engaging with schemes, focused on quality of decision making and contingency planning

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Any questions?

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Links to the documents

- Statement: http://www.thepensionsregulator.gov.uk/docs/db-annual-funding-statement-2015.pdf
- T10 analysis: http://www.thepensionsregulator.gov.uk/docs/db-analysis-tranche-ten-forward-2015.pdf
- T8 analysis: http://www.thepensionsregulator.gov.uk/docs/db-analysis-tranche-eight-review-2015.pdf

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