Quattro Pensions
CONSULTING ACTUARIES

news bulletin

Prospect House,
Fishing Line Road,
Redditch,
Worcestershire B97 6EW

Tel: 01527 598688

www.quattropensions.com

The Pensions Regulator's Post-Referendum Statement

Following the result of the referendum on 23 June 2016 to leave the European Union, the Pensions Regulator has issued a Statement to trustees and sponsors of pension schemes.

The Statement confirms that trustees, while needing to remain vigilant, should continue to take a considered approach with a focus on the longer term. Trustees and employers should discuss any changes to circumstances in an open and collaborative way and review their position as part of an integrated approach to risk management.

Employer Covenant

Trustees and employers should discuss the effects of the referendum on the business, taking into account the trading relationships, reliance on imports and exports, and changes in the strength of sterling. Trustees are encouraged to review their contingency plans.

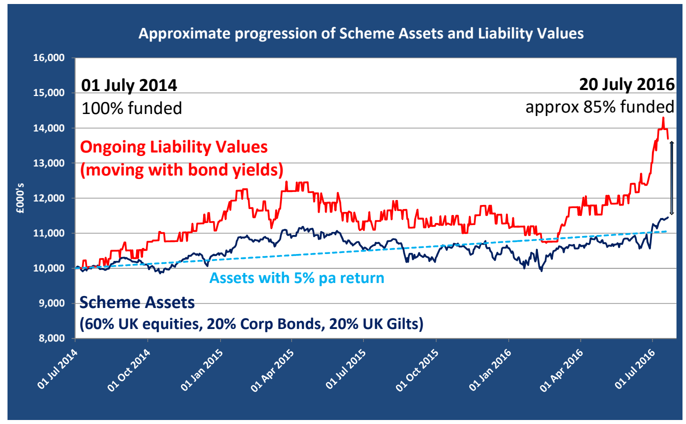
Investment Strategy

Trustees should not be overly focused on short-term market movements, other than for meeting cashflow requirements. Trustees should consider the potential impact on their long-term view of expected risk and returns, taking into account interest rate and inflation risks and currency exposures. If current conditions mean the scheme is exposed to an inappropriate level of risk, trustees should reconsider their investment strategy. If action is needed, trustees should consider timing and be ready to act when appropriate.

Scheme Funding

Trustees may wish to consider sensitivity analyses to understand the potential impacts of different scenarios on the scheme, and how this relates to the employer's ability to provide support. Funding solutions could be considered which incorporate more contingent security or conditional contributions with regular review periods, for example.

In summary, trustees will need to understand whether the referendum has had an impact on the employer's covenant and business plans, before making funding decisions. Except in crisis situations, it is the long-term rather than short term that is important, with regular monitoring.



Impact on Scheme funding

The graph illustrates how a scheme's ongoing funding position may have developed over the past two years. To measure liability values, this example scheme uses discount rates based on high quality bond yields. In July 2014, long-dated AA-rated bond yields were about 4.2% pa, and long-dated gilt yields about 3.4% pa. These yields are now down to 2.5% pa and 1.6% pa respectively, as investors seek 'safe' assets. The recent significant falls in yields have occurred even though credit-rating agencies have downgraded their view of the UK.

The fall in yields over the past two years has added significantly to a scheme's liability value on all measures. A scheme fully invested in gilts or LDI products would have seen significant positive asset performance to offset the rise in liability values (long-dated gilts have returned +45% over the two years). Schemes with such strategies may be able to secure some benefits with an insurance company.

In the example illustrated, 60% of the assets are in UK equities which have performed positively, even with the uncertainties surrounding the referendum, but not sufficiently to keep pace with liability values. 100% funded has become 85% funded over this two year period. (Schemes with different maturities and asset strategies will have performed differently.)

The extent to which the fall in yields is taken into account when valuing liabilities for scheme funding will depend on each scheme's circumstances and the strength of the employer's covenant, and whether any contingent security can be made available. Monitoring the employer's covenant may be particularly key at this time, as part of an integrated approach to risk management.

July 2016

Quattro Pensions Consulting Limited. Prospect House, Fishing Line Road, Redditch, Worcs. B97 6EW.
Tel: 01527 598688 Fax: 01527 598615 Email: info@quattropensions.com

www.quattropensions.com