



Managing Pension Risk

Evelyn Ryder

An increasing focus on pension risk

There has been increasing focus from:

- Investors, analysts and corporate management
- Scheme members
- The Pensions Board
- Numerous examples over recent years of poor risk management

Pension funds face a shortfall of billions

Regulator focuses on longevity projections
Companies to cover increased liabilities

By Norma Cohen

Companies face having to add billions of pounds to their pension liabilities under plans to be unveiled by the regulator to force them to use more realistic projections of how long workers will

known as PAR2 Modum Cohort, has fallen to out of line with actual experience that it can no longer be viewed as prudent.

“What we are saying is that while longevity is impossible to predict, we do believe that schemes are underestimating how longevity will continue to improve in the future,” said Charlie Massey, executive director at the Pensions Regulator.

The regulator is to issue a discussion document suggesting that scheme funding plans will

New methods needed to tackle fund deficits

SCHEME sponsors and trustees need to face up to the realities of deficits and consider

By Jonathan Stapleton

IBEC warns of threat to defined-benefit pensions

Daily Mail, Tuesday, May 24, 2005 Page 87

CITY COMMENT

Countdown to pension crisis

Alex Brummer

THE idea that an overhaul of Britain's pensions fund will have to wait until after the next election, irrespective of the recommendations of Adam Turner's commission, boggles the mind. Previous changes made to pensions almost always make matters worse.

Yet Gordon Brown and his advisors are adamant that no real and lasting change should take place until there is a national electoral and vote-buy support for reform.

The law review panel of the Pensions Protection Fund - the ruling law review panel in the House of Commons that is intended to review the status of future retirees in companies when an employer goes bankrupt - is a great political ally of those who will keep the pension system in its current state.

The degree to which the pension landscape has changed since 1997 is evident from a survey by Alex Brummer.

It has found that for the first time there are now more defined contribution or money purchase schemes open than traditional final salary plans. So far these defined contribution schemes have accumulated £26 in assets, which leaves gaps in the amount.

In the falling figures for the Turner Commission it has been found that half the employees entitled to join a defined contribution scheme have opted to do so. As a result half the workforce in these companies will have no private pension to look forward to and the liability falls back on the taxpayer.

The government is

What does remain in the hands of the pension funds is what it is in the hands of the state. It will be a major task for the state to resolve.

But there will also be concern that the state will be forced to pay for many European markets and to pay, even if pension schemes have reached saturation point with up to 100 per cent of the workforce in the state.

It is not clear whether the state will be able to pay for the state pension, which is the only way of meeting commitments to move these schemes with adequate provision for the state.

Now that Malcolm Collier has been appointed as chief executive of the state pension, it is clear that the state will be forced to pay for the state pension, which is the only way of meeting commitments to move these schemes with adequate provision for the state.

New fears on pensions deficits

Rules for assessing funds' future liabilities

Companies set to oppose proposals

By Jennifer Hughes and Norma Cohen

Company pension deficits could balloon under radical proposals to shake-up accounting rules.

The proposals by the UK Accounting Standards Board

The moves will attract opposition from companies who fear pressure to increase pension scheme funding. But it will be welcomed by investors seeking greater clarity on pension risks and activists lobbying for greater security for scheme members.

Ros Altman, a specialist in pensions economics, said that the new rules may discourage future defined benefit pension scheme provision. “Unfortunately, this may well frighten employers, but for so long we have treated

reduced by the returns expected on pension fund assets - typically benchmarked on the yield on AA-rated corporate bonds. The new proposals say companies should use the much more conservative measure of the “risk-free” rate, usually the yield on long-term government bonds.

If companies switched today to a risk-free rate, reported pension liabilities could rise by more than 20 per cent, experts said.

The ASB's proposals have

“The ostrich approach to pensions accounting hasn't worked. This is clearly unattractive for companies but we've got where we are today because no one wanted to face up to the issue.”

The move by the ASB comes as the International Accounting Standards Board gears up to launch its own shake-up.

Rules developed by the IASB are used or being adopted by more than 100 countries including the European Union, Japan,

IASB, it is a global leader in pensions accounting.

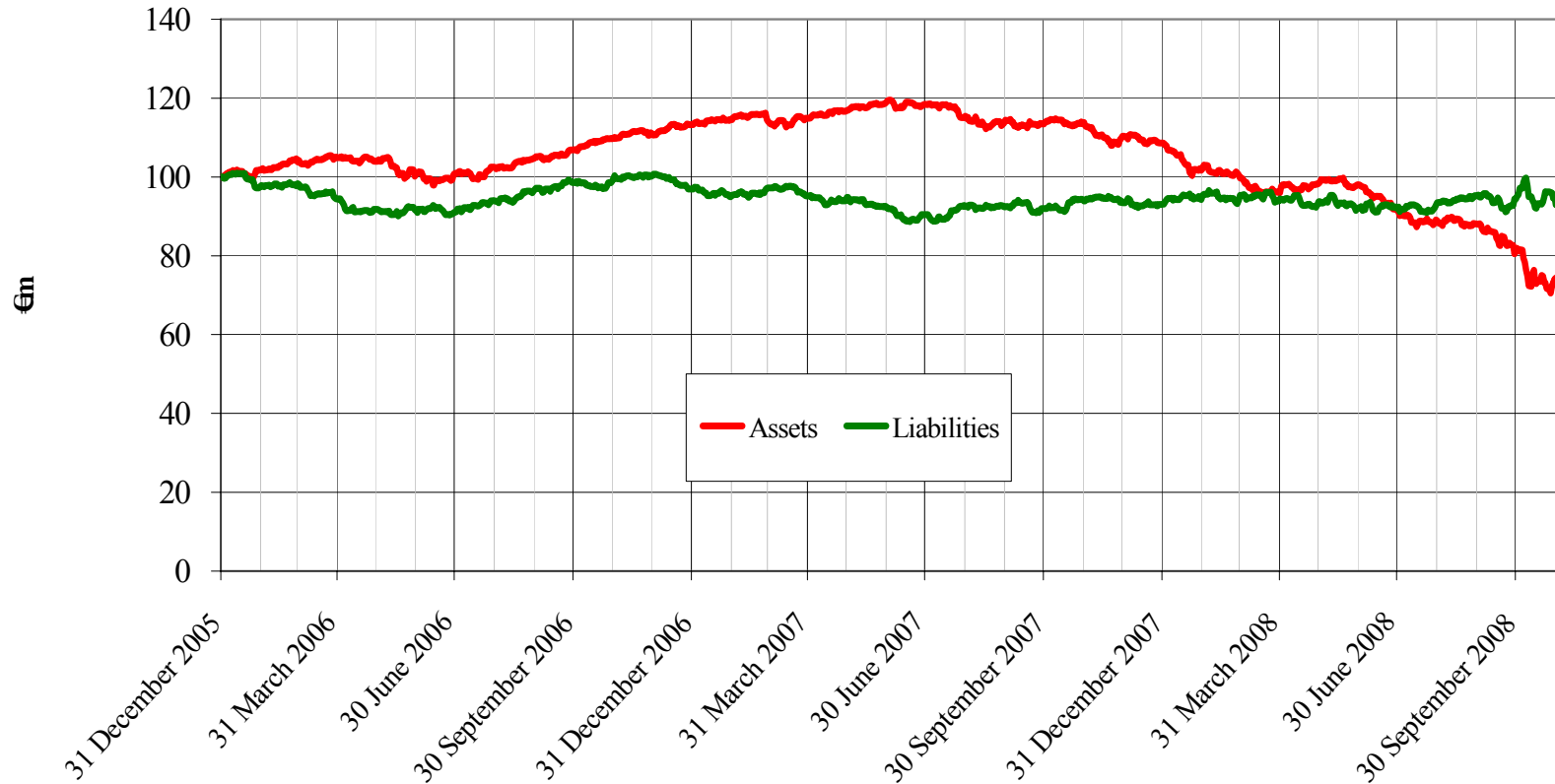
Pensions accounting has been controversial for years, particularly after the insolvency of employers whose schemes appeared fully funded on paper but in reality were not.

Analysts and investors are increasingly demanding “realistic” calculations of assets and liabilities. But the rules have been opposed by employers' groups who argue that pensions are a

Recent movements in your funding position



Asset and Ongoing Liability Projection



Note: The above graph is approximate, and becomes more approximate as the projection period lengthens. It reflects approximate stock market movements and interest rate changes (assuming these occur uniformly along the length of the yield curve), but not client-specific factors, such as material changes in membership numbers or profile or changes in benefit scales. It is designed to give a broad picture of the direction of funding changes since the last actuarial valuation but does not have the same level of reliability as, and therefore does not replace the need for, formal actuarial valuations.

What factors influence your attitude to pension risk?



- Contribution Volatility
- Member Reaction to change in benefit
- Accounting Volatility
 - P&L
 - Balance Sheet
 - Rating Agency Perception

How do Trustees/Sponsor define Pension Risk?



- Overall Risk Budget
- In isolation
- Peer Group Comparison
- Don't know?

How does one measure Pension Risk?



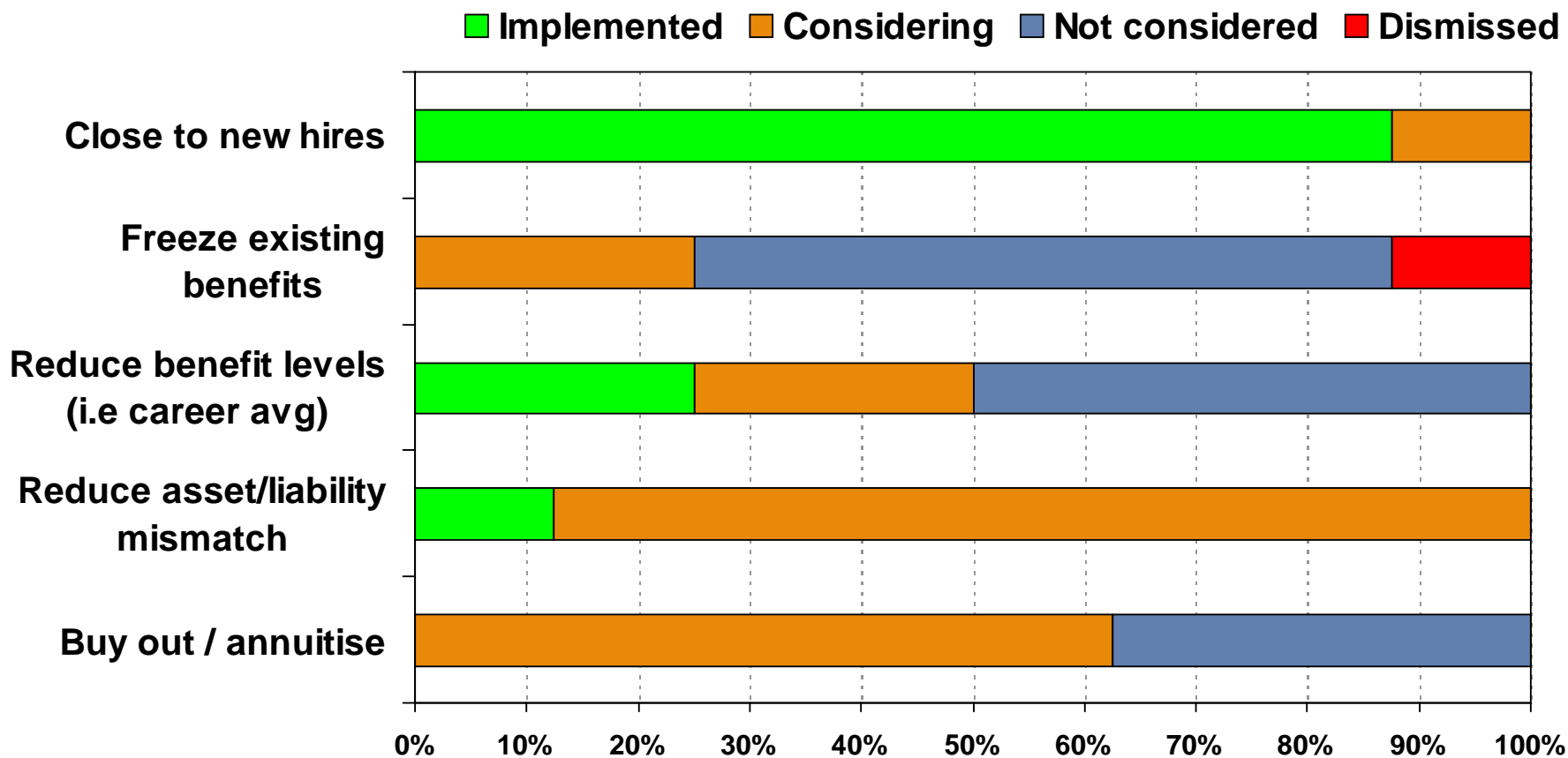
- Asset Liability Modelling Exercise
- Deterministic Shock
- Value at Risk Locally
- Value at Risk Globally for Multi-national



Main Risk Measures?

- Equity Investment Risk
- Inflation Risk
- Interest Rate Risk
- Longevity Risk
- Liquidity Risk
- Covenant Risk
- Operational Risk

Actions taken to deal with pension risk in Irish Schemes



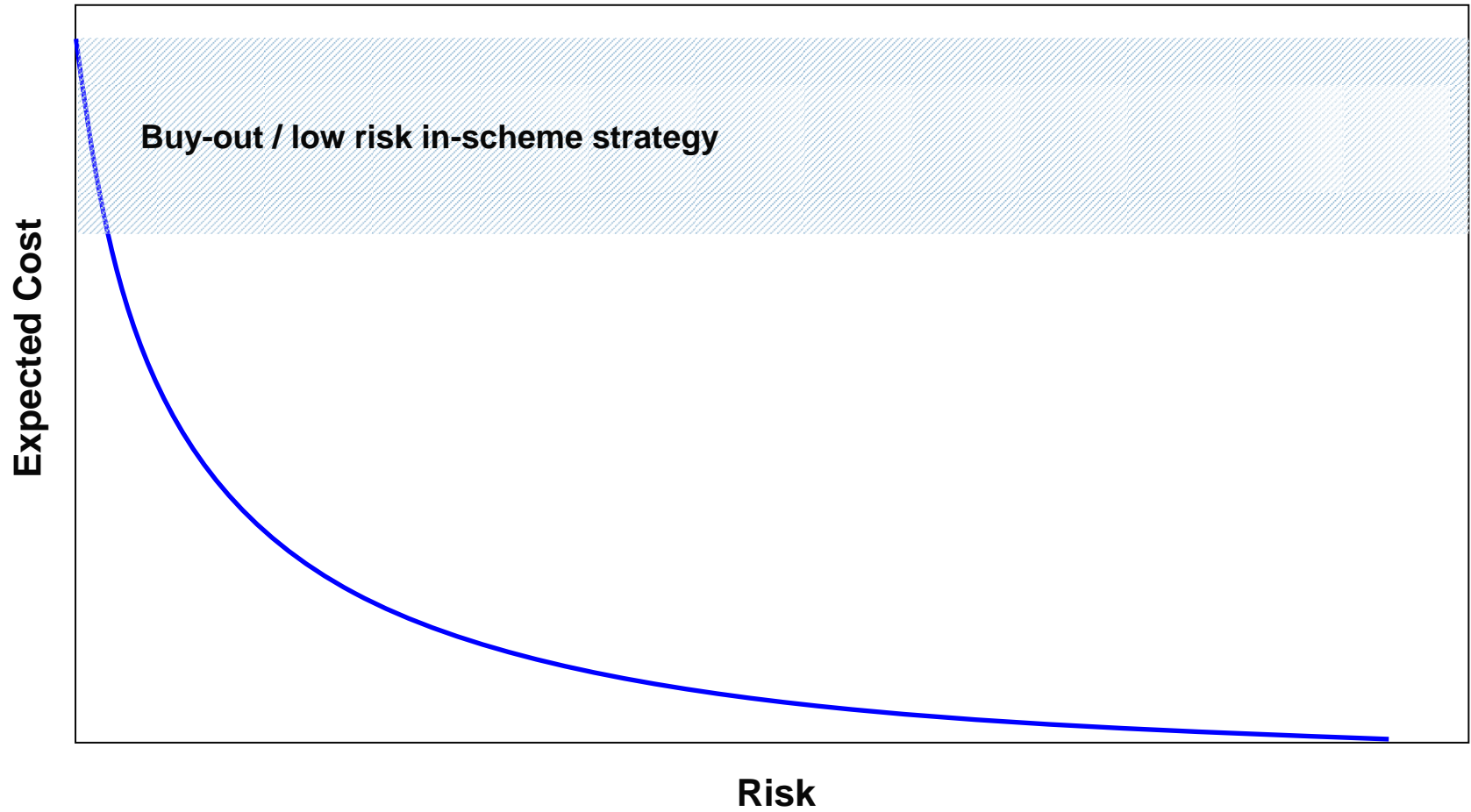
Liability Management Techniques



Opportunity for Actuarial Profession to show innovation and ability to manage Risk

- Normal Retirement Age
- Pension Increases
- Future Accrual
- Buy Out Options
- Enhanced Transfer Value
- Early Retirement
- Commutation
- Good housekeeping

The price of certainty



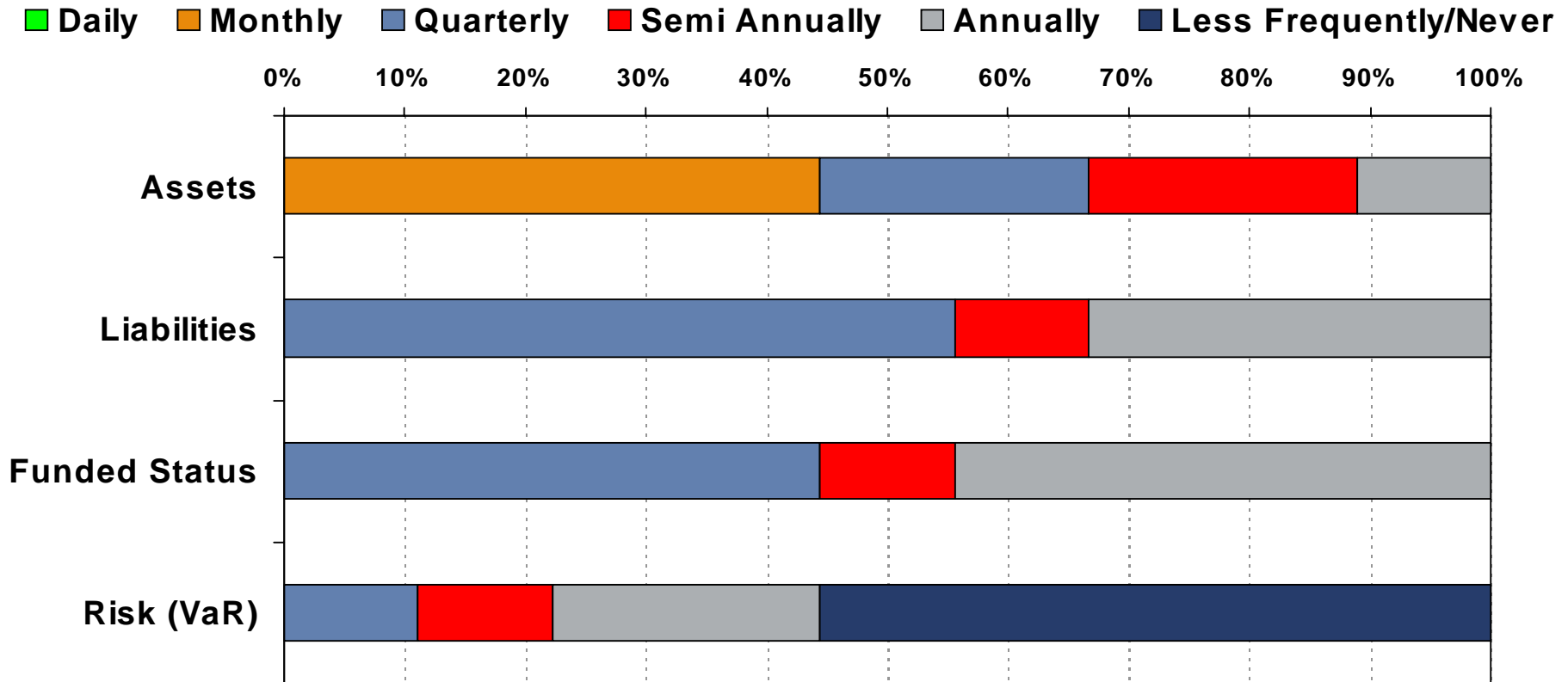


Asset Management Techniques

Opportunity for Actuarial Profession to show innovation and ability to manage Risk

- Concentration
 - Equity
 - Irish Equity
 - Irish Property
- Uncorrelated Assets
- Matching Assets
- Liquidity/Cashflow management
- Contingent Assets

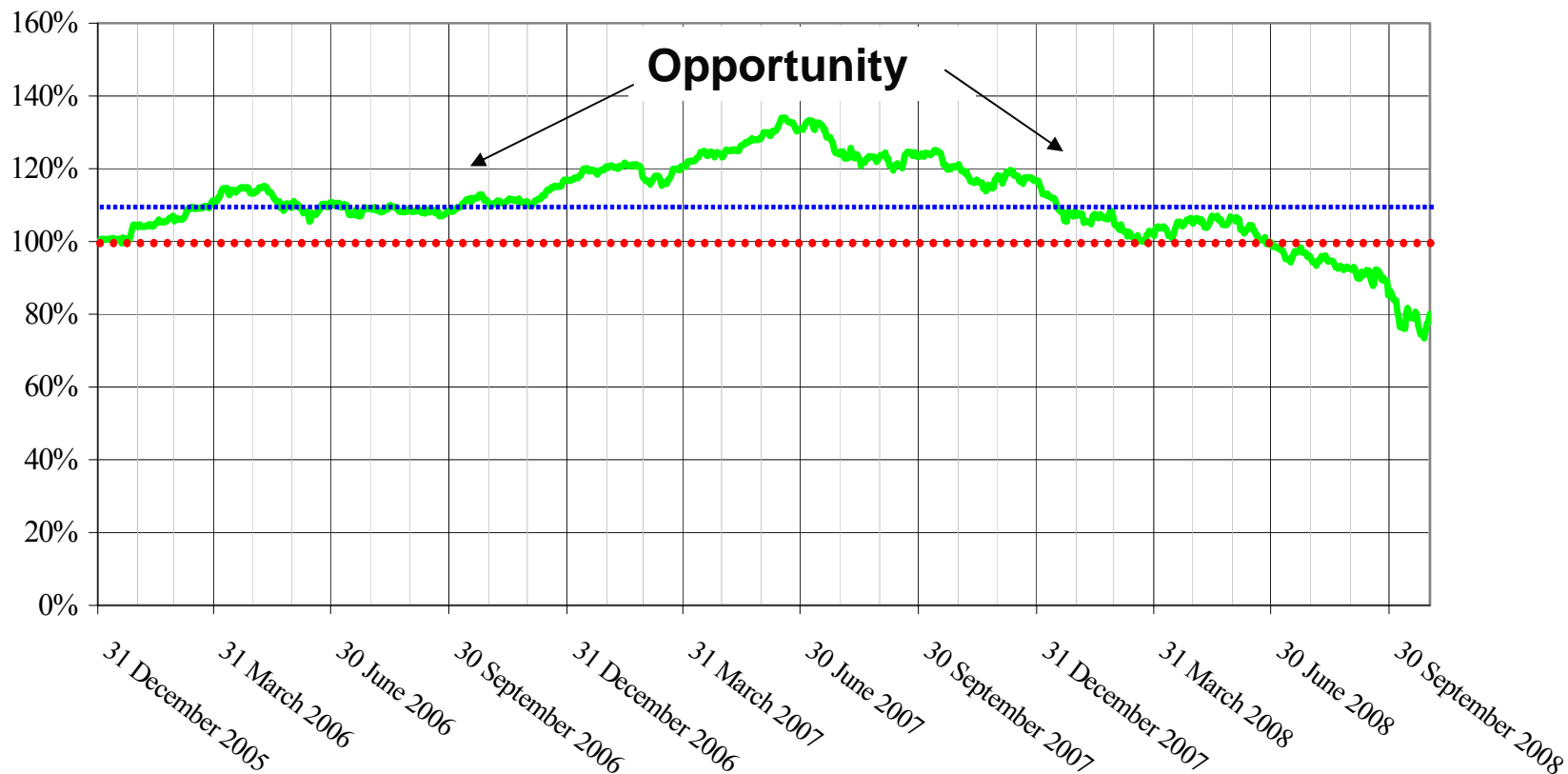
Frequency of Tracking/Monitoring/Managing Irish Schemes



Create and Recognise Opportunities to Reduce Risk



Ongoing Funding Ratio



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Create and Recognise Opportunities to Reduce Risk

