Pensions Aspects

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'Talking 'bout DC generation'

In the hot seat with Gareth Tancred

Engagement in a DC world

The biggest DB announcement of the decade

Pensions Management Institute
Moving pensions forward

In the hot seat with Gareth Tancred

With summer around the corner, PMI CEO Gareth Tancred delivers some early heat in this special extended edition of in the hot seat

Jason King: How did you find yourself in the pensions industry?

> **"I'm an accountant by profession, with a typical accountancy background. I got my qualifications, became a department manager, then a financial controller, then I got my first FD role when I was in my mid-thirties.**

Gareth Tancred: The organisation I was in at the time had a Defined Benefit problem, so my introduction to pensions was essentially a realisation that they weren't as easy as they should be. A bit later I also held a short role as a trustee, and I always found myself thinking, 'how do we solve this issue?'

That was quite difficult for me because I was the new kid on the block. A lot of the things that came up in meetings were just going way over my head. But that role gave me a far greater insight into how the industry worked.

One day, the phone rang with an opportunity to join a professional body. I went in as Chief Operating Officer, which I did for a couple of years. Then, the Chief Executive left, and the board asked me if I'd like to take over, so I did.

After five years, I'd delivered my strategic plan, the institute was in a lot better shape, and I decided it was time to consider what was next. So, seven years ago, I joined the PMI.

JK: Tell us a bit about Gareth Tancred

GT: I've been married for 37 years this year, I have three grown up children, one of whom has their own child, so I'm a grandfather as well.

I mentioned my traditional accountancy background, but I was never happy with just being an accountant, I've always thought to myself 'how can I get behind that, how can I help the organisation improve?'

> **"I was that annoying child who was always taking things apart trying to improve them. I was modifying the spokes of my bike, trying to make it sound like a racing car or motorbike, for example. That mentality followed me into my career.**

In some of the organisations I worked with I got a great deal of satisfaction from just walking around and talking to people in factories and such, trying to identify what challenges people face in real-time and working out how to solve them.

I've found that mindset of looking for constant improvement has really helped me get to where I am today.

I think a big part of me is just looking for new angles on things. I'm a little bit of a geek if I'm honest; I have a drone, and 've been doing a home automation project for the past 2 years, trying to automate pretty much everything.

I had a phase where I was into photography, and I guess the drone was an extension of that. I suppose my hobbies also reflect that sense of trying to see things from another perspective and get them to work better.

JK: What do you think is the biggest challenge the industry faces today?

GT: It's difficult to pick one single challenge, because there are so many. Clearly, a big one is getting the Dashboard across the line.

In many respects, the pensions industry is a little bit behind the curve in comparison to other areas in financial services. Banking and investment apps have made information such as balance and transaction history immediately accessible to consumers for some time.

The pensions industry really should have got to grips with offering that level of access by now, but we're getting there.

Even when we do get the dashboard to this first phase, you still won't really be able to do that much with it. It's really the next phase on from that where possibilities will truly start to open up.

JK: So, it will still be advisor driven, rather than being fully automated?

GT: Yes, exactly. And whilst you can find out what your pensions are worth, you've either got to go through emails or various bits of paper to try and work it all out yourself. The majority of people in the industry are financially literate and able to do that.

But the general population are less likely to, even though keeping track of your balance is extremely important. As an industry, we're only just getting to the stage where we're able to give people that information in a clearer, more accessible way.

Another challenge is that the industry is changing less quickly than society. Nowadays, where there are two spouses, both are typically earning an income, but they have childcare costs to consider. More people are self-employed or freelancing, particularly after the rise of the gig economy.

People also stay at jobs for much shorter periods, so you've got lots of little pots everywhere. Pensions provision must try to combine all of that.

JK: Would you say that dashboards can be part of that solution?

GT: I think so,

> “ **dashboards should help to open up a more sensible dialogue about pensions, providing a gateway to improving financial literacy and engagement.**

As a society we don't like paying for advice. We think that we know the answers, which is one of the reasons why people get into all sorts of trouble, because they don't want to pay a solicitor or similar.

But we do now have more flexibility of choices, and more diverse retirement outlooks, and we need to make sure that people are aware that they can lose a lot very quickly if they don't know what they're doing.

The dashboard can also help us to communicate these kinds of messages.

JK: Do you see PMI as being in a position to push the industry into keeping up with society?

GT: I think there is a role for organisations like ours, working with other, similar bodies to help the industry. We do that through some of our thought leadership and conference agendas, and the insights we provide.

We pride ourselves in championing the collaborative energy that provides the right solutions for consumers. Realistically, we'll never have enough scale as a professional body to be able to be consumer facing, but we can help those firms who are consumer facing cope with the everyday issues, concerns and changes in society as they come along.

JK: As a self-professed tech geek, are you excited and/or worried about the emergence of AI?

GT: It's a little bit of both. We have used it within the organisation in strategic planning sessions. We were looking at market demographics and stuff like that, and we found it very helpful as a research tool.

It does currently come with a few health warnings. For example, the dataset isn't always up to date. But if you work around some of those health warnings, I think AI could really help, and our organisation could definitely use it more.

Having said that,

> “ **with every invention, somebody will find a nefarious use for it. Scams in the pensions industry are already huge, so AI worries us in that respect.**

If you can get ChatGPT to write a script, and another sophisticated AI to put a realistic face and voice to it, you could very easily create a very convincing scam. And, as the pots are so big in pensions, scammers would only need to succeed a few times.

We're also concerned about the implications it could have on jobs. Automation has been around for a while – the motor industry has had robots for decades – but we're now at a stage where artificial intelligence is able to think for itself, make decisions by itself, which makes jobs in the financial services more precarious.

We also have to make sure people aren't using AI to get an unfair advantage over other students in exams, as the answers it generates can be pretty convincing. We put this to the test by having our Director of Lifelong Learning, Keith Hoodless write questions, and our policy director and tutor, Tim Middleton, come up with a model answer.

Then we asked ChatGPT to come up with an answer, and it would have scored highly. That's a problem, because we're trying to test someone's application of knowledge, not their ability to go to a machine and find the answer.

JK: In terms of the modernisation, you've already moved the PMI brand on so far. What's next?

GT: Well, we have a five-pillar strategy. The first pillar is taking what we already have and simplifying it for growth.

Historically, we've had quite a complicated and convoluted exam structure and more membership grades than most professional bodies. Some of those grades were related to the exams you took, meaning you'd find yourself at a dead end. We've re-engineered all of that, launching what we call Pathways in April.

Pathways doesn't just favour one particular section of the industry, so regardless of where you are or what you want to do there will now be a far more inclusive way to get to your associateship or fellowship.

Our member grade structure has also been simplified to make it easier for people to follow, and there's still more simplification that we plan to do.

Pillars two and three are about new products and services, and we'll be making some announcements on those later in the year. What I can tell you now is that we've got some new ideas that will help learners, members and corporate partners.

The fourth pillar is about markets. We've been looking at geographical and demographical markets, and we want to do more to try and help people come into the profession.

Lastly, pillar five is about understanding who we are, what our purpose is now, and redefining our purpose for the future, and that will come with a bit of a new look and feel as well.

Simultaneously, we need to look at our governance, how we operate, and make sure that we're working as effectively as possible.

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Membership update

Your membership, what's happening?

Membership Renewal

Your 2023-2024 membership becomes due on **1st September 2023**. Renewal notifications have been sent out to all student, professional (ProfPMI), Associate (APMI), and Fellow (FPMI) members.

If you have not received your invoice please contact us at membership@pensions-pmi.org.uk

PMI Membership Fees 23/24

Membership Category	Fees 2023/24
Student	£178
Professional	£255
Associate	£385
Fellow	£475
Retired/Non-Working	£75

Continuing Professional Development (CPD) non-completers

Fellows and Associates are reminded that their 2022 CPD becomes due on **1st January 2023**. Meeting the PMI CPD requirement is compulsory (except where retired/non-working). Under our CPD Scheme, PMI members are required to record **at least 25 hours** during the year. Please log on to your member portal and update your CPD record.

Failure to have completed the required CPD for three consecutive years (without having notified the PMI of any extenuating circumstances) will result in your membership being downgraded and you will lose your entitlement to exclusive APMI and FPMI member benefits such as the use of your designations, voting rights and opportunity to be elected to PMI's governing structures.

We strongly urge all our APMI and FPMI members to use our online CPD recording tool available through the My PMI member portal.

If you wish to record a self-declaration for CPD completed under the auspices of another professional institute, please download the self-declaration form from here and return this to membership@pensions-pmi.org.uk

CIPP Affiliate Membership

Know of a colleague with both Pension and Payroll-specific duties?

We have partnered with the Chartered Institute of Payroll Professionals (CIPP) to deliver enhanced value for members from both institutes. The partnership will support those with payroll and pension functions in their role and help those wishing to expand their own professional understanding of both these areas.

PMI benefits include:-

- Digital copy of Pensions Aspects (PMI bi-monthly magazine)
- PMI Technical News (technical supplements)
- Pension-specific collateral
- Discounted rates for PMI training courses and events. See here for a full list.
- Access to PMI webinars
- Access to PMI Regional groups
- Opportunity to join PMI's Mentoring and Development Programme
- HMCA member discounts
- Access to Pension Careers – Online job board

CIPP benefits include:-

- Access to CIPP Advisory Service – 12 enquiries per year
- Online Professional in Payroll, Pensions and Reward magazine
- Discounted rates on CIPP events. See here for a full list.
- Discounted rates on CIPP training courses. See here for a full list.
- Payroll-specific collateral
- Networking opportunities on CIPP's Specialist Interest Group
- Access to CIPP's payroll jobs board
- Free attendance at online BeKnowledgeable webinars

Get in touch with the membership team for more details at membership@pensions-pmi.org.uk

Congratulations to all our recent upgraders

We are pleased to announce that the following members are now entitled to use the designatory initials **"ProfPMI"**.

Veneta Petrova	Stefanie Ives	Lauren Neal
Paresh Pandya	Gareth Orr	Paula King
Charlotte Hart	Kimiya Farjadifar	Lorraine Goodison
Rachael Iley	Emily Caines	Jayne Sanderson
Zoe Cheng	Phillip Shurmer	Claire Goddard
Rebecca Fearnley	Catherine Laycock	Emma George
Catherine Fitzgerald	Nilesh Hirani	Carl Hague
Anna Griffin	Troy Finch	Porsche McLaughlan
Nicola Nevers	Daniel Curtis	

We are pleased to announce that the following member has been upgraded to Associate and can use the designatory initial "**APMI**".

Robert Jenkinson

PMI Regional Group News

London Regional Group Update

Martin Lacey
Communications, PMI London Regional Group

The PMI London Group hopes all our members are having an enjoyable summer!

We held a successful business meeting in May, where we were delighted to welcome Kerrin Rosenberg (CEO, Cardano Investment), Alasdair Macdonald (Head of Investment Strategy UK, WTW) and Donny Hay (Director, IC Select) to discuss the LDI liquidity crisis. Jonathan Gilmour (Partner, Travers Smith LLP) chaired an interesting and thought-provoking debate. The London Group would like to thank our guests for their insights and Travers Smith LLP for their hospitality in hosting the event. It was really nice to see so many of our members after the business meeting for networking over drinks and nibbles!

At the time of writing we're busy preparing for our Annual General Meeting in June. We're really looking forward to welcoming Sir Steve Webb (Partner, LCP) who will be speaking with Amanda Burden (Board Director, Pi Partnership Group) for a "fireside chat" that will delve into the many challenges that currently face the pensions industry and opportunities for the future. The London Group would like to thank Aon for their hospitality in hosting our AGM.

Remember to keep an eye out for details of our upcoming social events and business meetings via the PMI London Group LinkedIn Group.

PMI Regional Group News

Southwest Regional Group Update

Katie Lambert
Communications, PMI Southwest Regional Group

The PMI Southwest Regional Dinner will be held on Thursday 7 September, Harbour Hotel, 53-55 Corn Street, Bristol, BS1 1HT.

Tickets cost £60 and a £5 donation will be made to Age UK, our chosen charity, for each ticket sold.

Please book your individual place, half table of 5 or table of 10 via Eventbrite: https://pmi-south-west-dinner-2023.eventbrite.co.uk

PMI Events

The view ahead for PMI Events 2023

PMI is hosting a range of pensions-industry-leading events for 2023. With industry specialists delivering the best insights and knowledge to flagship events such as The Pinnacle Awards, excellent networking opportunities and extensive partner exhibition and sponsorship packages. For further details please select from the list below or see pensions-pmi.org.uk/events for the full programme.

18 - 19 Sept 2023
Introduction to Pensions (Basic)

20 - 21 Sept 2023
Introduction to Pensions (Advanced)

25 - 27 Sept 2023
Secretary to the Trustee (Basic)

28 - 29 Sept 2023
Secretary to the Trustee (Advanced)

4 October 2023
PensTech & Admin Summit (virtual)

12 Oct 2023
Retirement Matters Training Taster Session

2 Nov 2023
Trustee Workbench

23 Nov 2023
The Pinnacle Awards

7 Dec 2023
ESG and Climate Summit

ITM Student Essay
Competition 2023

PMI 9th student essay competition winner

Sponsored By
itm
Solution delivered...

In addition to policy mandated by government, what can the pensions industry do to make a real difference in the battle against climate change?

James Turner
Senior Pensions Administrator, Quantum Advisory LLP

Introduction

Climate change! The threat to our way of life and perhaps very existence. The greatest danger to humanity (with the possible exception of the war in Ukraine) since the end of hostilities in 1945. It is something that none of us can escape or ignore, both personally and professionally. In fact, it can be argued that the pensions industry is affected by climate change more than most, both in the potential impact but also in the ability to tackle the problem.

Pensions are all about the future, and the impact of climate change is likely to only get worse as time goes on if we do not step up to stop it. However, the largest asset that most people own is their pension (with the possible exception of their property) and thus the industry as a whole has a unique amount of power to affect policy and outcome, given the enormous assets for which it is custodian. The following explores just a few of the ways in which this change could be brought about.

Pension industry working practices

The first and perhaps most obvious way the pensions industry can help to tackle climate change is to adapt its working practices towards greener policies. This is by no means limited to the pensions industry, but for pension-orientated companies that tend to hire a medium to large-scale workforce (with some of the larger insurance firms employing thousands of staff), their contribution can make a difference.

COVID-19 started a trend of moving towards a less office-based working environment, which has almost certainly had large positive environmental impacts. Working from home means fewer journeys to and from the workplace, less need to heat or, in the much less likely scenario of the UK having warm weather, keep cool large office spaces and a move to paperless working (i.e. almost everything being kept on internal computer systems without the need to print forests of paper) are just a few examples of this positive environmental change. If pension firms can continue with the change and even improve on it (for example by encouraging cycle-to-work schemes or car-sharing arrangements when it is necessary to travel to the office) an important step towards fighting climate change will have been taken.

Also, there is an opportunity for the pensions industry to alter the way it meets disclosure requirements when it comes to scheme member communications. Many communications are still sent as bulk postal deliveries, simply because this is how it has always been done. However, if the method of sending was switched to electronic communication via email or the internet, it would save not only the paper/printing environmental cost but also the pollution produced from the delivery vehicles needed to send physical copies. Changes can also be made by greater use of electronic signatures (for example for investment instructions) and removing the need for scheme members to sign forms when possible. Naturally, a balance must be struck between environmental concerns and member security. It would also be necessary to ensure members who could not access electronic communications could still receive postal copies. However, with technology's ever increaseing reach into our lives, fewer and fewer people are dependent on such communication methods.[1]

[1] Forbes website: https://www.forbes.com/sites/forbestechcouncil/2021/05/11/the-sustainable-impact-of-a-paperless-office/?sh=71b33a591095
[2] ONS website: https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/fundedoccupationalpensionschemesintheuk/julytoseptember2022
[3] Pension Age website: https://www.pensionsage.com/pa/Green-pension-21x-more-effective-than-common-climate-efforts-combined.php
[4] FCA website: https://www.fca.org.uk/data/retirement-income-market-data-2021-22#key

ESG investing (part 1) – greater use of positive screening

Environmental, social and governance (ESG) has been a cornerstone of the pension industry (especially the investment aspect) for quite some time. In 2019, scheme trustees were first required to state their ESG considerations in their statement of investment principles, and the ESG consideration requirements have only increased since. This is of particular importance, as according to the ONS the market value of defined benefit and hybrid pension scheme was c.£1.45 trillion on 30 June 2022. This is a sizable market share in itself, but when it is considered that these types of pension scheme now account for less of the total industry share than in the past (with defined contribution pension schemes becoming the norm for most occupational and all private pensions), the assets under the management of the whole pensions industry are enormous and growing. As such, the pensions industry can command considerable influence in this area.

There is a considerable push towards 'negative' screening when it comes to investment opportunities (i.e. taking steps to remove shares in companies, for example that actively do harm and fail ESG criteria by causing too much pollution, from portfolios). However, a greater impact could be achieved by encouraging more 'positive' screening, whereby scheme trustees and their investment advisers actively seek ESG-friendly investment opportunities.

The positive environmental impact of such a strategy could be limitless. Greater investment in companies that promote action against climate change would naturally help the environmental cause by increasing the assets/funding available to such companies. In itself this would be useful but money has a way of attracting money. As such, initial investments by scheme trustees adopting 'positive' screening will surely encourage other investors to put their money in such assets. All that is needed are a few trend-setters to start.[2]

ESG investment (part 2) – invest where it will make a difference

It is sometimes perhaps a forgotten fact when it comes to pension investments, where the main goal is (and should be of course) the achievement of strong and sustainable growth for scheme members, that there is huge potential for the recipients of the investments (i.e. the companies into which pension investments purchase shares/stakes).

Many pension investment strategies are centred around medium to large companies in developed economies such as the US or Europe. However, there could be massive benefits if scheme members had more opportunity to invest in smaller and developing economies to allow some of the capital to help meet their growth needs. Pension investments used to build cleaner power stations (as one example) in the developing world would have obvious environmental advantages and could potentially lead to larger returns given the increased perceived risk of the investment.

Once started, the process would have a compounding effect, as these countries would become richer and naturally move towards greener policies and practices. This has been the trend ever since the industrial revolution; as a nation increases its wealth, it becomes more environmentally friendly both because it can better afford to do so and because its population demands it to improve their standard of living. In addition, there is strong evidence that ESG and sustainable investing practices are what scheme members want and expect.[3]

Annuity providers and annuitant lifestyle choices

Although the annuity has somewhat fallen in popularity since the introduction of Pension Freedoms in 2015, a large number of annuities continue to be purchased, with over 68,500 being secured in 2021/22. This may well increase in the short term due to favourable market factors (such as higher interest rates).

It is well established that annuity providers will offer better rates based on lifestyle choices but these have traditionally been based on poor health/lifestyle circumstances. If annuity providers could be persuaded to offer higher income for a person who makes positive environmental choices (such as opting for walking over driving when possible), then Adam Smith's 'invisible hand' could gently guide retirees into helping combat climate change. The difficulty with this policy would be making it worthwhile and profitable for the annuity providers. However, many companies make decisions based on environmental considerations, so they benefit from positive public perception of these actions. This might be possible in the annuity sector and might be a key deciding factor in a person's decision to purchase an annuity with one particular provider over another.[4]

Conclusion

Climate change is a problem that affects us all, and the pensions industry is no exception. There are many ways in which the industry can make a difference to the fight against climate change, of which only a few have been explored here. They vary from basic changes in the way companies involved in the industry operate and communicate with their scheme members, to larger changes in the industry's arguably most powerful tool when it comes to influencing policy: the investment market.

The key to effecting large-scale change in the medium to long term will be to gently nudge people's behaviours and attitudes and to educate them in the positives that their pension (particularly its investments) can have for the environment. The industry as a whole will also need to learn these lessons and take actions in addition to those that government and regulatory bodies mandate. Otherwise, it may well soon be too late and the fight against climate change could be lost forever.

Insight Partner Article

Bridging the Gap:

Navigating Post-Retirement Challenges in Defined Contribution ("DC") Schemes

Britt Hoffman-Jones
Head of Master Trust, Schroders Solutions

September 2022 will go down etched in memory given the significant movements in gilt yields. There was a great deal of attention on the impact this had on Defined Benefit ("DB") schemes, and in particular a focus on Liability Driven Investments ("LDI"). Following these events several industry bodies have been lobbying to receive a complete picture of the types of investments used in DB schemes. The consequences for DC members during this period, however, has not garnered similar attention, nor has it resulted in the same level of industry 'call to action'.

A member retiring from a DC scheme in early October 2022 will have experienced significant volatility and potentially crystalised a loss at the point of retirement. This emphasises the need to better align the retirement journey, creating a stronger bridge that connects members from pre-retirement to post-retirement.

The impact of crystallisation at retirement

In DC schemes, the single most important decision is still made by members when their pot is at its largest, and seemingly where they may have the least support – at the point of retirement. The point of crystallisation involves converting accumulated pension savings into a retirement income stream. A member typically achieves this by taking a cash lump sum, purchasing an annuity, or entering some form of drawdown arrangement.

One key risk associated with crystallisation is the timing of the decision. Pension savings can be subject to market volatility, and if individuals are forced to crystallise their pots during a market downturn, it can have a detrimental effect on their retirement income.

For illustration, let's consider a member with a c.£300,000 retirement pot as of 30 June 2022 invested 30% in equities, 35% in fixed income and 25% in cash. If this member crystallised their pension pot on 11 October 2022, they would have incurred a loss of c.£15,000. Whereas if the same member remained invested until February 2023, they would have achieved a gain of c.£10,000 from their 30 June 2022 value. The impact of this timing would have resulted in a difference of £25,000 for the member.[1] This further highlights the impact decisions at-retirement can have on member outcomes, particularly when volatile market events can lead to little time for members to make up losses.

Of course, there are alternative options available to members, such as purchasing an annuity. Whilst providing a guaranteed income for life, this may not offer the flexibility or potential for growth that some retirees desire. This, combined with rates being unattractive over the past decade, created a perception that annuity rates offered poor value, causing individuals to be cautious about committing to this option. Although annuity rates have significantly improved over the last 18 months, the perception of poor value remains well-established with members.

To address this challenge, at Schroders Solutions we are working closely with several pension schemes to create a post-retirement solution through a Master Trust. This solution removes the point of crystallisation for members at retirement. To achieve this, we align the pre-and post investment strategy, creating a mirror of the investment strategy that members invest in as they approach their target retirement age within the Master Trust.

Aligning the pre-retirement strategy with a post-retirement bolt-on

Aligning the pre-retirement strategy with a post-retirement bolt-on addresses the challenges and risks associated with crystallisation at retirement. This approach offers several benefits:

1. **Re-registration of units to remove out of market risk:** As the strategies are fully aligned, it does not require the need to "sell and buy units" and instead a process can be adopted that removes all out of market exposure, and importantly the "cliff edge" point of crystallisation.
2. **Comprehensive retirement planning:** By incorporating the post-retirement solution into the overall retirement strategy, individuals can engage in comprehensive retirement planning. This involves considering both the accumulation and decumulation phases of their pension savings, allowing them to make informed decisions about contributions, investment choices and risk.
3. **Access to enhanced benefits:** Integrating a post-retirement bolt-on within a Master Trust offers access to a broader range of benefits and services beyond traditional retirement income solutions. These benefits can include engagement apps, interactive tools, and educational resources that empower individuals to make more informed decisions.
4. **Cost efficiency:** Aligning the pre-retirement strategy with a post-retirement bolt-on allows individuals to benefit from cost efficiencies and economies of scale. Members can continue to benefit from cost savings received in pre-retirement into their post-retirement strategy. This cost efficiency maximises the value of individuals' retirement savings and has the potential to improve retirement outcomes.
5. **Improved member engagement:** The alignment of pre-retirement and post-retirement strategies offers an opportunity to enhance member engagement throughout the retirement journey, allowing members to better recognise and understand their investments. This can be built on further by utilising technology-enabled solutions, which can encourage greater personalisation, encouraging active participation, promoting financial education, and empowering individuals to take control of their financial wellbeing.

Removing the 'cliff edge' of crystallisation associated with DC at the point of retirement is crucial for better serving the aspirations of DC scheme members. By bridging the gap and addressing post-retirement challenges, members can achieve a more secure and fulfilling journey, laying great foundations to build on personalisation. The industry must focus on providing innovative solutions, supported by regulatory changes, to empower individuals to navigate the complexities of managing their accumulated wealth, of which workplace DC will be a significant contributor.

[1] Source: Schroders Solutions. For illustrative purposes only.

Pension communications: is it plain sailing or leaving members all at sea? | Insight Partner Article

Insight Partner Article

Pension communications:

is it plain sailing or leaving members all at sea?

Steph Gold
Principal and DrumRoll Lead Consultant, Barnett Waddingham

Getting members on board

Member engagement - it's a phrase we're hearing more and more when it comes to communicating about pensions. This is probably because a communication shouldn't just be telling members important information we think they should hear, it should be about increasing their interaction and gaining feedback so they feel involved.

No longer can the industry simply throw members in at the deep end and hope they can swim. We need to give them the tools to navigate their journey to retirement, keeping them informed and engaged along the way. It's a two-way process, not a one-way channel.

So, what does effective engagement look like?

First and foremost, it should lead to members taking positive action. Whether that's a member making decisions for their here and now or planning for their future, effective engagement doesn't just happen.

Secondly, it needs to be accessible for everyone, accommodating all member's needs. This includes (but isn't exclusive to) members with low levels of numeracy or literacy skills, those who are visually impaired and those deemed vulnerable by the Financial Conduct Authority's (FCA) new Consumer Duty.

All hands on deck

Pensions are essentially a long-term investment vessel and must be treated accordingly. But those involved in the industry know how challenging it is to make sure members understand and value their pension, and are engaged in planning for their retirement.

We need to have clear, pro-active and involving communications throughout each stage of a member's journey to retirement, providing relevant information they can actually understand.

At DrumRoll, we believe effective communication starts with a seamless marriage of engaging copy and design. It must be straightforward and you guessed it - accessible and inclusive to everyone..

It's simple - well-informed and engaged members take responsibility and make better decisions.

Consideration needs to be given to a variety of mediums including written materials (generic and personalised), webinars, videos, face-to-face communications and digital solutions, such as email alerts and an online member/ employee portal. Maintaining a balance between the digital world and the human touch is paramount.

So how do we do this?

- Make it really clear what the purpose of the communication is, with the key message front and centre on the first page.
- Keep the introduction short, friendly and reassuring so the member is more likely to read on!
- Provide clear instruction on what the member needs to do next, with navigation (signposting) on where to get more help.
- More detailed information is separated out in guides so they can cherry-pick the relevant information they need, with more generic information in simple, well-designed flyers.
- Incorporate a range of design elements to complement these principles including clear visual signposting, wider margins for device readers, single columns where possible, left-aligned justified text and carefully chosen font styles to name a few.

Communications should be designed to be adaptable, so if there are specific requirements for larger fonts, colour theme changes or alternative formats this can be accommodated.

Include various means for members to provide feedback, actively encouraging and promoting it. Finding out what works and what doesn't only aids in further driving engagement.

Rocking the boat

We need to be aware that different individuals have vastly different approaches to retirement planning. For each member that takes a proactive and curious approach to their pension, there will be many others who are uncertain, uninterested or completely unaware of their benefits.

It's entirely possible that without encouragement, members will only consider their pension needs at the very brink of retirement – too close to the storm, when it might be too late to make the necessary provision required for a secure and happy retirement. Think more desert island than island paradise.

Providing effective messaging to a diverse group of individuals can only be accomplished by a high standard of accessible and inclusive communications.

These individuals will be at different stages in their lives and will have differing interest levels in pensions, so we need to tailor our messaging accordingly. You can do this by identifying members by age cohort, gender and occupation, and then use the most appropriate tone/language and means of communication for that audience.

It's the duty of the trustees, working together with their 'crew' - administrators and other stakeholders - to make sure the information provided cements itself in a member's consciousness. This will give them the greatest opportunity to understand the options available to them and, if necessary, take action going forwards.

Sink or swim

Every member should know when and how they can access their pension and be sufficiently engaged throughout their journey. They should be well informed about which course might be best for them to navigate and, in line with the Stronger Nudge introduced by the Government and FCA, should know where to go if they need some guidance or advice.

They should also be given opportunities to provide feedback, which in turn enables the industry to evolve and meet changing demands. Effective and engaging retirement journeys should be for everyone. Otherwise we risk leaving members high and dry, having received communications which are anything but shipshape.

Find out more about Barnett Waddingham's award-winning creative communications constultancy team, DrumRoll, at **https://drumrollcreative.com**

Insight Partner Article

Financial guidance for the DC Generation

Andrew Harper
Associate, Sackers

Defined contribution pensions are a minefield for savers. Today's generation of pension savers are faced with myriad different decisions to make, often without any support.

Questions like "how much should I contribute?", "what funds should I invest in?", "how should I withdraw my money in retirement?" and "do I need advice, and if so from whom?" weigh on the minds of those who want to achieve good retirement outcomes. Or worse – savers don't know that these questions need to be thought about at all!

Savers need help in understanding the issues they face when planning for retirement. Getting these questions right can have a substantial impact on someone's financial wellbeing in retirement, and the consequences of getting it wrong land squarely on the individual.

Despite increasing demand to do so, pensions and retirement planning are not yet taught in schools, and there is an overall dearth of mainstream education on pensions. At the same time, relying on pensions knowledge being passed down from family or shared in a social setting is an exercise in pot-luck, and taking independent advice can be expensive. This gap in knowledge has been acknowledged by regulators in recent years, but many people are still not armed with the knowledge they need to properly tackle these pension decisions.

So what can employers, trustees and providers do to help their employees and members?

Worried about "giving advice"?

There is often a concern shared by trustees and employers that providing some kind of guidance might cause them to be inadvertently providing "advice" and fall foul of FCA regulations. This is not an un-warranted concern, as performing a regulated activity like providing regulated advice without FCA authorisation is a criminal offence.

The FCA has acknowledged concerns around providing support to savers, without crossing into advice, and has committed to a review of the boundary between advice and guidance. However, in the meantime, there is a relatively clear line between the "advice" which cannot be provided, and "guidance" which any organisation can offer. The key is not to provide personalised recommendations, or any information which is tailored to an individual's own circumstances and financial aims. Certain options should not be put forward as "the right one", nor should any particular product be promoted over others. Instead, the focus should be on giving factual information about general principles, like explaining different types of investments or different ways of accessing pension benefits.

TPR and the FCA have issued joint guidance in recent years relating to how employers or trustees can provide support without crossing into giving advice. This guidance is a helpful starting point and indicates that these bodies consider that trustees and employers can be doing more to help.

What about the risk of not doing anything at all?

Whilst the provision of guidance rather than advice is a line to tread carefully, and there is no clear legal duty for trustees or employers to provide guidance, there are good reasons why employers / trustees might decide not to rest on their laurels.

The legislative landscape has changed substantially towards a more paternalistic regime, with the introduction of automatic enrolment, the protective transfer conditions regime, and initiatives like the nudge to guidance. TPR is taking a similar stance, expecting DC trustees to provide additional context and materials with annual benefit statements. Looking at this path of change, there is a risk that simply offering access to pension saving may not be enough going forwards.

From an employer perspective, the view could be taken that by not providing support they are allowing employees to sleep-walk into poor decisions. This could lead to reputational damage or complaints being raised which then have to be dealt with, particularly given the increased focus now on employee wellbeing, which includes their financial wellbeing.

Start small and work from there

In terms of what support to offer, a starting point is to simply signpost individuals to other forms of guidance which is already available, like the free and impartial services of Pension Wise or MaPS. Communications to pension scheme members, such as annual benefit statements, or employer communications like an employee-benefits website, could be updated to highlight these resources.

Doing more than this can be a little more complex to put in place, requiring a process of due diligence, as well as a consideration of costs, and may require legal advice to ensure you don't stray into giving advice. However, there remains a menu of different options, so organisations can pick what would be suitable for them.

A step up from signposting guidance is to engage with a financial education provider who can provide slightly more targeted education. This could range from workshops for those still accumulating, robo-advice on an on-going basis, to one-to-one sessions at retirement.

Other options include pointing people to a list of regulated advisers who can provide personalised advice, or selecting a regulated adviser, or a panel of them, to provide personalised advice.

So, a range of options exist for helping employees and members to make better financial decisions about their futures, without going as far as giving "advice". Providing a degree of additional guidance may require a little bit of bravery, but could make a big difference to the DC generation.

Insight Partner Article

Engagement in a DC world

Sharon Bellingham
Master Trust Lead, Scottish Widows

Living in a household of three young digital native "Zoomers" (or "Gen Z"), I have hands-on experience of the challenges around engaging with an audience who see more of their phone screens than they do their family.

My three Zoomers are already very different when it comes to attitudes to money and savings, with the spectrum ranging from frivolous spending all the way through to frugality. The influence of personality type is already apparent, as is the preferred method for receiving information – some of us prefer to use our mobile phones whilst others might prefer speaking to someone. This tells us that hyper-personalisation is key and inclusive design is at the heart of engagement and ensures diverse needs are met.

Understanding Different Engagement Needs

In our most recent Master Trust member survey, we found that 40% of our members have three or more pension pots, and 42% of our members think an online platform with all their pensions in one place would stimulate greater engagement. With the recent Pensions Dashboards update confirming a new connection deadline, we're poised and ready for action and are excited by the opportunity dashboards provide through showing clear, simple and secure information about every type of pension in one place – this will rapidly transform retirement planning and overall pension engagement.

Our survey also told us that for Gen Z and Millennial members seeing everything in one place was the most important thing to help them better connect with their pension, and will help them feel a greater sense of pension ownership.[1] Being part of Lloyds Banking Group means that Lloyds, Halifax and Bank of Scotland customers can see their Scottish Widows pension alongside their bank account, and our data tells us that most of us look at our bank accounts twenty-six times a month (which is almost every day). So, this provides a significant opportunity to reimagine retirement savings as a 'current account for your future', alongside other financial products.

As a natural progression from Open Banking and the development of Dashboards, Open Finance will further revolutionise how people engage with their finances. AI will play a significant role in enhancing engagement by anticipating members' needs and providing personalised communication and behavioural nudges, helping members make informed decisions and encourage thinking about long-term savings. And as people's needs evolve throughout their lifetime, these solutions will naturally flex and adapt around their changing priorities.

Consumer Duty, with its mandate for driving better understanding and outcomes for consumers, will also be a catalyst for positive change. There is, however, also a risk that it creates an engagement disparity in the industry and a two-tier pension communication landscape; not all pension products and schemes are in scope and even just considering the Master Trust market, some providers (such as Scottish Widows) are implementing the higher and clearer standards that Consumer Duty requires, whilst others are not required to.

The Engagement Journey

It's important that employers, trustees and pension providers adapt to Generation DC's needs in order to ensure the right balance when engaging with members about their retirement savings. Sensitively educating to enable savers to manage finances using new technology is key to helping members make informed decisions on what matters now, as well as future financial resilience. There remains, however, a significant place for in-person support, often delivered in the workplace; in our experience this continues to be incredibly popular and highly valued by members.

We also have a fantastic opportunity to support younger generations, to help them to learn about finances – embedding a positive savings culture at an early age is an important early intervention and will help influence financial outcomes. My youngest Zoomer once posed a question to me, asking, "At school, why don't they teach you how to pay for life?", and it's certainly a key point and something that's even obvious to a much younger generation.

The Money and Pensions Service (MaPS) have funded financial education in schools programmes. This, and other industry initiatives, including our own Lloyds Bank Academy, are examples of how we can empower young people with financial skills. But it's clear that more is needed to integrate and firmly embed financial education across national curriculums. Helping people grasp the basic building blocks of pensions and investing is key – and to achieve this, we need a system that leaves nobody behind and supports people to be money-confident and prepare sufficiently for retirement.

It's clear that we have a considerable pensions engagement gap, where fear and detachment is the sentiment that many people have towards their retirement savings. But we have a huge opportunity, through data science and personalisation, to bring the 'current account for your future' to where people already are. We can connect using simple and inclusive language, that reflects where people are in their retirement journey.

Engagement, however, is only step one. Once we have people's attention, we need a laser focus on providing the seamless help members need to make informed decisions and to make the changes now that will be life-altering to their financial future.

[1] According to research from Scottish Widows, Scottish Widows Master Trust Member Survey 2023.

Insight Partner Article

What role can language play in helping Generation DC pension scheme members contribute the right amount for them?

Mary Cahani
Director,
UK Institutional, Invesco

Stephen Messenger
Head of UK Strategic Institutions, Invesco

The UK's auto enrolment system is now well established. Millions more employees are contributing to workplace pensions. Yet engagement in retirement saving is as low as ever. For Generation DC, few have moved beyond the default contribution levels that were set for them by the government. To achieve financial security in later life many will need to contribute more than the minimum.

Research conducted by Invesco, Nest Insight and language strategy experts maslansky + partners has helped identify some of the barriers to engagement with pensions, and understand how simple changes to the language used to talk about saving could help scheme members overcome them.

One of the reasons why pensions auto-enrolment has been successful is because at its heart it harnesses people's inertia. Yet this same inertia is the thing that's standing in the way of people engaging with their levels of saving.

In our research, we looked at whether better use of language can help overcome some of the barriers that stand in people's way when they try to consider their savings choices. We reviewed the language the industry uses to talk about the money people save, and the actions they can take, and tested different forms of language that might help them navigate around these blocks and barriers.

The aim of this is to identify practical approaches that can deliver positive behavioural outcomes for DC scheme members. The research questions we set out to answer were:

1. How do DC members understand pension contributions currently – what are the comprehension and awareness barriers to engagement and action?
2. How can language and message framing around contributions be better used to help improve the success of interventions designed to help people to save the right amount for them in retirement?

We combined three different research methods - expert interviews, qualitative and quantitative research - and applied innovative methodologies including the use of Emotional Response dial technology.

DC pension scheme language research – how we did it

8
industry expert interviews to identify perceived barriers to engagement, best practices and desirable outcomes

33
UK pension savers in four focus groups, to gauge responses to barriers and evolve the language that helps to overcome them

1,500
more UK pension savers surveyed to validate and quantify our learnings

Key themes and findings

We began by looking at the significant barriers DC scheme members face when they try to engage with their contributions. The automatic nature of enrolment, and the default contribution settings, have set up powerful anchors that bind people to the status quo. On the flip side, there is much that is off-putting about the nature of pensions information, including too much use of technical language and difficult concepts like percentages. The industry has also not always been good at answering the question 'what's in it for me?' around engaging with contributions.

What are the barriers to engagement?

2 out of 5 didn't know they can choose how much they pay into their pension	1 in 3 think minimum contribution rates are a recommended level of savings	2 in 3 said they have left their contributions at the default savings rate	1 in 3 weren't aware that their employer also pays into their pension

Next, we identified some foundational messages that can help fill common shortfalls in people's knowledge and understanding:

1. 'You can contribute more to your pension'
2. 'You can make a difference to your financial security in later life by rethinking the amount you contribute to your pension'
3. 'Contributions you make when you are younger work harder for you'

We then explored a range of different versions of key messages about contributing to a pension. By making granular comparisons between different approaches we were able to see big differences in the level of comprehension and engagement that can be achieved by saying the same thing in a different way.

Our findings fit within a framework where communications should be Positive, Plausible, Plain spoken and Personal:

Positive
Positivity is a powerful tool in building engagement. It is also, perhaps, an under-used approach in communications about retirement saving. Too often, these can focus on what people are not doing or how they are missing out. For instance, messages about gains resonate more than those about avoiding loss. A 'you can' is more likely to engage than a 'you should'. And messages that highlight the benefits of 'free money' and 'growth' are more powerful than those about contributing the right amount or taking responsibility.

Personal
Messages should be framed from the individual's point of view, rather than the scheme's or employer's perspective. Messages that used the words 'you' and 'yours' are more engaging than messages that used the words 'our', 'company' or 'members'. Language can be more powerful if it helps people recognise they are on a 'default setting' – and suggests they move from this by customising their retirement savings around their personal situations.

Plausible
It might be tempting to try to motivate people to save by painting a picture of an aspirational future. Yet employees are resolutely pragmatic about retirement saving. Credible framing of the benefits of saving is more likely to connect than visions of a 'dream' retirement. 'Financial security' is more motivating than 'financial independence'. The idea of 'security' is known to be an important part of financial wellbeing. It may also be particularly salient in a time of great uncertainty.

Plain spoken
Technical language creates barriers to engagement. Plain-spoken alternatives attract more interest amongst pension scheme members. That said, the word 'contribution' seems to work for them, in spite of some negative connotations. Still, they need clear, plain-language explanations to understand what contributions are and how they work. Generation DC are also more interested in hearing about what they will get out than what they put in. And when it comes to retirement outcomes, it's important to present these in terms of pounds-and-pence income, rather than talking about final pot values or percentages.

Messages for change

In line with the framework set out above, our research identifies that messaging around pensions should be 'Positive, Plausible, Plain spoken and Personal'. For example:

POSITIVE	PLAUSIBLE	PLAIN SPOKEN	PERSONAL
✓ If you take action, you could be on track for a comfortable retirement	✓ Financial security	✓ Contributions	✓ Create a personalised savings plan that fits with your vision of retirement
✗ If you do not take action, you could be at risk of outliving your money	✗ Financial independence	✗ Retirement salary Investments Savings	✗ Create a savings plan that stays in line with how peers your age are saving

Finally, we explored whether certain moments or methods of communication are more effective in boosting engagement and nudging people beyond the defaults. We found that milestones in the workplace and in personal finances appear to be more relevant than personal milestones. It was also noted that the pension provider is most expected and trusted to provide information to people. However, a significant proportion of employees see this as the employer's role, particularly younger workers.

Continued from page 5

In the hot seat

with Gareth Tancred

JK: More generally, how would you describe your time as CEO of PMI?

GT:

> "There's never a dull moment.

Sometimes switching from one particular issue to another to another several times a day can be difficult, but that's part of the excitement.

I suppose one of the challenges in professional bodies is having a very wide stakeholder base. You're talking to many people on a day-to-day basis: your team, boards, committees, the council. There's a journey that you all have to go on together.

Then you've got your external stakeholders. There's a big industry out there with lots of organisations to talk to, and, of course, Westminster and the media.

When I came to PMI, I could see a lot of opportunities, but bringing everyone along on that journey has taken a while. We're only just beginning to do some of the things that I would have wanted to do earlier.

An example of that is the Pinnacle Awards, which is something that I wanted to do from day one. We weren't ready for it as an organisation at the time, but I'm glad that we're in the stage now where we were able to create something so special.

It's very different from the other awards ceremonies in the industry, and we designed it that way, so it has that educational, informative, and prestigious.

JK: Which of your achievements are you most proud of?

GT: I'm really proud of the fact that we responded very quickly for our members and learners in COVID.

There was a report recently that 2/3 of professional bodies like ours have lower income now than they did before COVID. 1/4 of them are facing going concern issues. We aren't.

Like most companies, we had a bad year during the early part of the COVID pandemic. When the initial lockdown happened, we faced losing the Spring exams and a season of face-to-face events. Our strategy was to look at when members and learners needed, and how we could help them.

> "We had already been looking at putting our exams online, so we accelerated that. Within six weeks of the first lockdown, all our students were able to take their exams at home.

From the first lockdown until the end of 2020, we also held around 120 webinars, providing plenty of opportunities for our members to get CPD, and some great channels for our corporate partners to get their insights out. We'd also lessened the requirements to get CPD, so it was a win-win for everybody.

Post-pandemic, our membership has grown, we're back to pre-pandemic student levels, and we have a much stronger balance sheet than we did even before COVID.

> "We bucked the trend to the point where organisations are asking us "how did you do that?" We've had regulators like OFQUAL – we're OFQUAL regulated – looking at us as a good example of how to come through COVID.

The other point I'm really proud of is our Pathways programme. It's a very significant change to what we've done for the last 47 years.

Before, people would come up to me at a conference and say "I just did this particular exam, what should I do next?" It would be so hard to answer that question because you'd have to understand all they'd done so far before you could give any advice as to what to do next.

You'd have to say "well what is it that you're doing, what is the career path you've chosen and what are you hoping to get out of it?"

It's now so much easier for people to follow a particular path. If they change their career, let's say they moved to a different company, that's fine. You can move from one pathway to another, take whatever non-common exams you need and press on to completion..

It was a very collaborative process, and we spent a long time thinking it through. Our members had a large amount of input, we did several surveys to get the views of our members.

> "I was really proud when one or two of our stakeholders told me this is the best thing to come out of PMI in years.

I hope to be able to continue to deliver moments like that.

PMI Activities

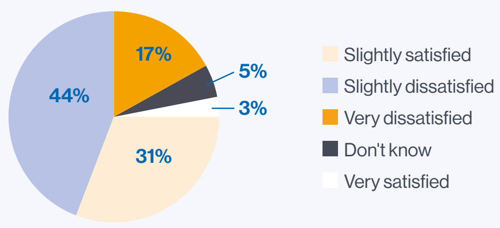
Summary of the first PMI Pulse Survey 2023

Tim Middleton
Director of Policy and External Affairs, PMI

There have been some significant developments since PMI's last Pulse survey. Long-serving Pensions Minister Guy Opperman resigned, was re-appointed and then moved to a new role. Laura Trott has now had several months in post and is now implementing her own vision for the role. At the Pensions Regulator (TPR), both CEO Charles Counsell and Policy Director David Fairs have also moved on, and a new era for TPR has begun to unfold.

The most visible development in workplace pension provision was the LDI crisis of the Autumn of 2022: a painful experience which raised some searching questions about the technical knowledge of trustee boards and the robustness of regulation. The launch of the dashboard scheduled for April has been deferred, and whilst this was generally seen as an inevitable development, it is still seen as a significant policy failure. Finally – and controversially – Chancellor Jeremy Hunt abolished the Lifetime Allowance (LTA) in his March Budget.

How satisfied have you been with the direction of pensions policy over the last six months?

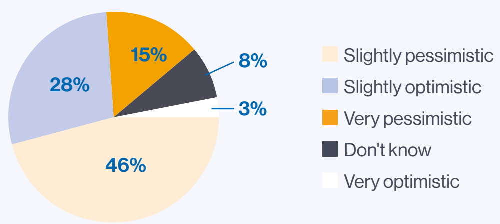


As with previous surveys, the first Pulse of 2023 began with the established series of questions about the role of TPR and the general direction of pensions policy. Given the disruption at the end of 2022, these questions generated some bruising responses.

Nearly two-thirds of respondents were dissatisfied with the general direction of pensions policy. This shows a marked deterioration since our last survey, when just 44% of respondents took a similar view. Comments from respondents were uncompromising:

- The financial and political upheaval of the last six months means pensions have been forced to the sidelines.

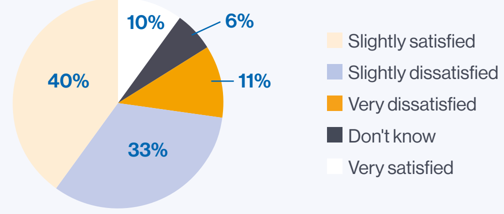
How optimistic are you about the direction of pensions policy over the next six months?



Again, nearly two-thirds of respondents were pessimistic about development of policy over the near future, and this shows a worsening of confidence since our last Pulse. One respondent commented:

- I think GMPE and pensions dashboards will be very challenging for many schemes and providers. The PDP is behind schedule but the compliance dates are very close.

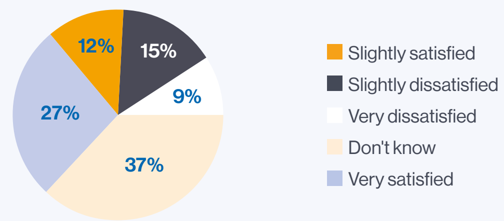
How satisfied have you been with the actions of the Pensions Regulator over the last six months?



Nearly half of respondents were dissatisfied with the performance of the Regulator. Again, this figure has worsened significantly since the previous survey. Comments from respondents included the following:

- Slow to react to key events, i.e. the gilt market volatility experienced during Sept/Oct.
- I don't believe TPR reacted quickly enough to the cost-of-living crisis, especially with regards to reducing, or stopping, their pension contributions.

How confident are you that The Pensions Regulator will focus on the right areas in the next six months?



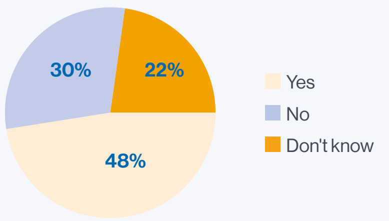
The number of respondents who were pessimistic has more than doubled since the previous survey. Critical comments included the following:

- Little chance of a change unless there is a serious change of both direction and personnel.
- TPR needs to get over the LDI debacle as soon as possible so that it can focus on the future

PMI Activities

The remainder of the questions in the survey were new, and focused on topical issues addressing the industry. The first of these was:

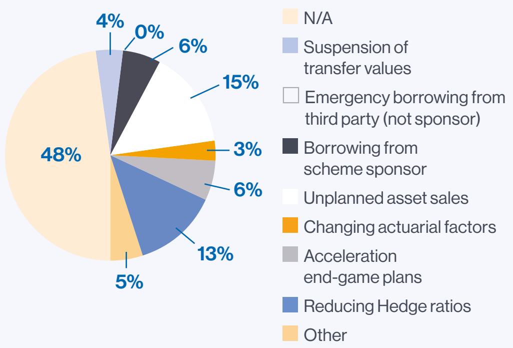
Has your scheme had to take action in response to turmoil in the gilts market?



The high number of respondents answering 'yes' is a clear indication of the widespread disruption that hit Defined Benefit schemes toward the end of last year. Comments from respondents included the following:

- No gilt sales were needed - there was sufficient liquidity to meet any margin calls. But I don't know (yet) as to whether a future-protective review has taken place.

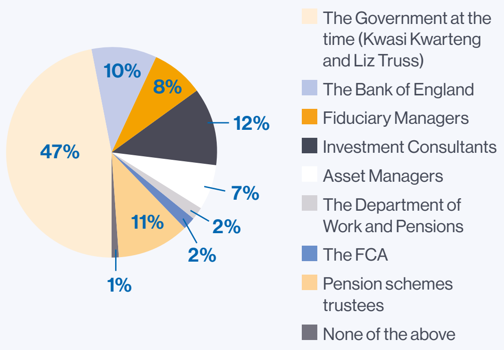
If your answer to the previous question was 'yes,' what action has your scheme taken?



Almost half of all respondents reported unplanned asset sales, which is a clear indication of the scale of disruption experienced by DB schemes. Comments from respondents included the following:

- Contingent sponsor support increased (not actually accessed but set up if needed), rejig of investments, reduction in leverage (not hedges), acceleration of end-game plans.
- Borrowed from scheme sponsor, unplanned asset sales, accelerated end-game plans.

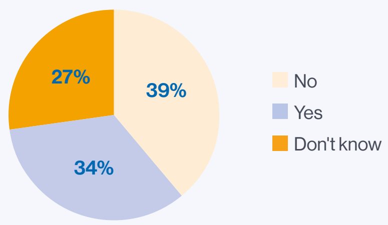
Who do you think was to blame for the turmoil in the gilt markets?



Clearly, respondents were dissatisfied at the brief but dramatic regime of Liz Truss and Kwasi Kwarteng. Comments included the following:

- Government for unfunded and non-credible budget. Bank of England for not adapting asset sale program / letting gilts run off / not tightening monetary policy sooner. Regulators for not understanding risks associated with concentration of gilt holdings and implications.
- Mainly the government, but many trustees were led by consultants too easily into leveraged LDI without thinking it through or stress-testing it properly.

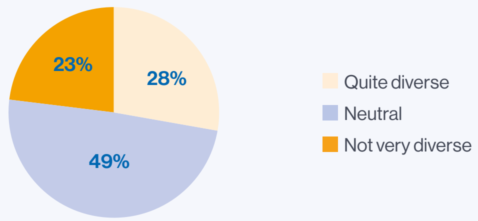
Are you concerned about anything within The Pensions Regulator's draft DB funding regulations?



This question prompted an inconclusive response, with an even split between the three options. One comment was:

- I agree with the basic idea of having a fast track to reduce reviews and concentrate resources. I disagree with TPR having any prescriptive funding strategy, asset return measure or low-dependency templates. If TPR wants to take over setting funding in this way you might as well sack all the trustees and transfer the assets to PPF. Doing what they propose risks groupthink yet again and that was one of the issues with LDI - everyone was buying the same assets so when they needed to be sold there were no buyers as everyone wanted to sell.

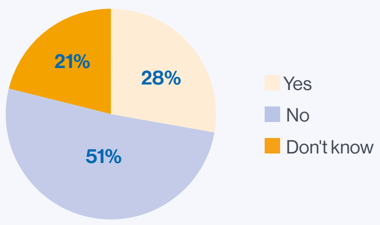
To what extent could your trustee board be described as diverse?



This prompted another inconclusive response. One response read:

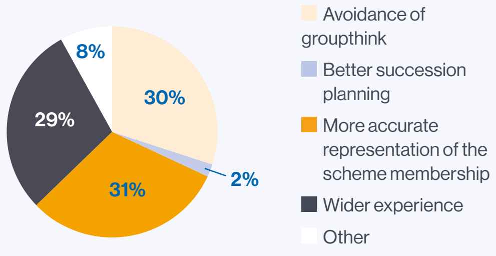
- We struggle to get trustees both Employer and Employee so selecting for diversity really doesn't happen. We try to major on life experiences which make us the person we are today in order to demonstrate our diversity.

Does your board have an Equality, Diversity and Inclusion (ED&I) policy?



The response to this question was consistent with responses to the previous question. It is perhaps a cause for concern however that half of those who responded report that their board does not have an ED&I policy at all.

What do you see as the principal benefits of a diverse trustee board?



Given that half of respondents had reported that their scheme did not have an ED&I policy, it was noteworthy that so many saw the benefits of diversity on a trustee board. One comment was

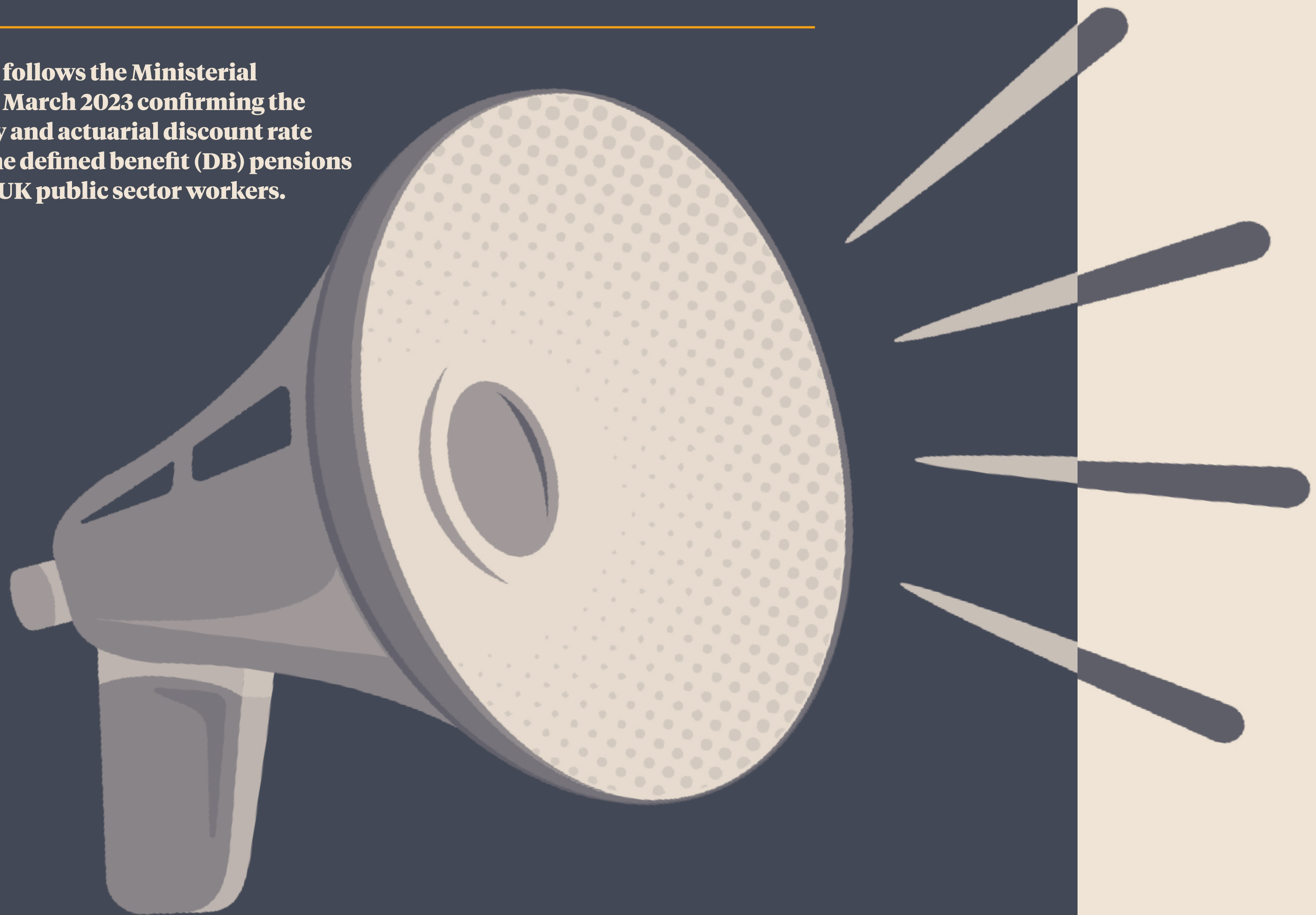
- Better decision making, better discussions about decisions

Feature Article

The biggest defined benefit (DB) announcement of the decade

Allan Martin
Director, ACMCA Ltd

Allen Martin follows the Ministerial Statement in March 2023 confirming the methodology and actuarial discount rate for costing the defined benefit (DB) pensions for 5 million UK public sector workers.



The methodology remains based on the assumed growth in the economy - the tax base from which benefits are paid in future, as measured by gross domestic product (GDP). The SCAPE (Superannuation Contributions Adjusted for Past Experience) discount rate (used to calculate benefits and contributions and retirement ages) has however been reduced from CPI+2.4% to CPI+1.7% pa. I suggest it is the most unappreciated but important actuarial assumption in the country. As a DC contributor, had you heard of this DB crucial assumption? Has your MP? The minister acknowledges that this reduction will lead to significant employer contribution increases in the delayed 2020 actuarial valuations, but these will be cost-neutral in department budgets, i.e. fudged.

In practice the biggest immediate financial impact will be on private sector employers participating in the public sector schemes, like independent schools. Equivalent increased employee contributions, a later retirement age or reduced benefits might not have been so easily explained! It is only an April 2024 ~£8bn pa deferred pay cost increase or recognition! That didn't get mentioned in the Budget. I'm sure any actual, potential or perceived conflicts of interest were appropriately addressed.

These deferred pay DB promises are for over 5m hugely deserving public sector employees, not just those finishing a night shift. Our Whole of Government Accounts (2020, latest available) put this accrued unfunded liability at £2,100 bn. The "fund" is the UK economy from which taxation will be levied in future. Just like funded private sector DB schemes, if the economy or fund doesn't grow as expected something has to give – higher contributions/taxes or lower benefits or later retirement. Squeezing individual government department budgets arguably equates to longer NHS waiting lists, bigger school classes, less officers on the beat, fires left to burn etc. You may speculate on the political likelihood of any change ahead of a general election - turkeys and Christmas may cross your mind!

The public sector benefits were previously promised assuming real GDP growth of 3.5% - 2.4% pa. GDP growth at such rates hasn't been achieved since the 2008-09 financial crisis and we have of course had Brexit, C19 and the war in Ukraine affecting actual and prospective growth. This suggests a consequential and massive intergenerational transfer of liability to future taxpayers - you, your children and grandchildren (if they don't emigrate).

Future taxpayers will increasingly only have their DC pensions savings, but they are effectively underwriting and belatedly contributing to these DB pension promises, a massive intergenerational transfer. Generation Z paying for their own DC pots and topping up historic DB pensions based on unachieved GDP growth. Unlike the currently temporary State Pension "triple lock" these DB promises are a "lifetime pensions lock". Sadly the initiating June 2021 Consultation and Response failed to address any aspect of past service experience and whilst the lower discount rate for future benefits is a step in the right direction, we still have a "lifetime (not triple) pensions lock" on £2.1tn of index-linked pension promises assuming GDP growth averaging CPI+3%. That 3% average real growth assumed, minus 1.7% now expected, every year over say 35 years on a (2020) liability of £2.1tn suggests the biggest DB deficit admission in UK pensions history; ~£500bn? Does this prompt an arithmetic comparison to a Ponzi scheme? DB pyramid selling is fine until you run out of DC buyers.

The long term GDP projection is taken from an Office for Budget Responsibility (OBR) July 2022 Fiscal Risks and Sustainability Report. Not much has happened since then! The "long-term" view was crucial with the 2018 SCAPE change (when the OBR projection for 2018-28 was ignored). A look at the more recent OBR Economic and Fiscal Outlook will provide lots more areas of potential concern and material risk, e.g. levels of migration, impacts of climate change and sustainability. Whether you are a parent, grandparent, a future tax payer or a now uncapped DC saver, you are picking up this tab and underwriting the risks.

For the economists – what is the difference between repayment of index-linked gilts and paying public sector pensions? The answer is at least "5m votes!" In addition the coupons on the latter are higher and they are paid for much longer.

The solution surely involves a necessary link of public sector deferred pay to achieved GDP growth; "sharing and rewarding" are the politically attractive words that might be used, "affordability and sustainability", less so.

Feature Article

How Collective Defined Contribution schemes can work for individuals and the economy

Matthew Eyton-Jones
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For many years now, there has been a broad consensus that defined benefit pension schemes are a legacy of the past that will die out with the last of their beneficiaries. Young people entering employment in the 2020s are just the latest cohort of 'Generation DC': their pensions schemes are almost invariably defined contribution schemes.

No one pretends the shift to DC schemes is a simple matter of progress. If anything, it fits more easily into a narrative of economic decline. Defined benefit schemes peaked in the late 1960s and have been steadily falling in size and number since the 1970s. For some, the move to DC is part of a package of raw deals faced by younger generations coming in the wake of the privileged Baby Boomers, from the student debt burden to the difficulty of getting onto the housing ladder.

It's true that the demise of DB can be seen as something of a rude awakening. Structural changes to the economy showed up the naivety of guaranteeing certain outcomes regardless of the performance of the funds meant to pay for them. Nevertheless, DC need not be seen as a raw deal.

Certainly, there is nothing unfair about each individual having their own pension pot. While its performance will depend on investment returns and their employer's contributions, as well as their own contributions, this is at least transparent.

The future of DC looks like being more complicated, however. Many experts now advocate merging the thousands of pension schemes operating in the UK into a few 'superfunds'. The immediate rationale for this is to obtain better returns for savers. Larger funds, such as those already operating in Australia and Canada, are able to make large-scale investments in a wider range of potentially high-yielding assets. For some, this is key to unlocking the potential of DC and providing savers with a retirement closer to that anticipated by their parents and grandparents.

Another benefit of consolidating funds is the ability to invest in long-term illiquid assets like infrastructure, private equity, and venture capital. This could not only result in attractive long-term yields, but would also be a boost to the UK economy, at a time when investment in infrastructure and innovation is sorely needed.

The basic point remains, though, that there are numerous advantages to consolidating schemes into larger funds, and not just the opportunity to invest in a wider range of assets. Regulatory pressures are also pushing many smaller, single employer schemes to join Master Trusts, for example. In particular, the Pensions Regulator's 'value for money assessments' have put an extra burden on trustees of smaller schemes, encouraging many to transfer to a Master Trust for an easier life.

In fact, it should be noted that some proposals seem more motivated by this latter benefit than by returns for savers. Chancellor Jeremy Hunt said in April that UK pensions were in need of 'urgent reform', emphasising the desirability of their investing in infrastructure and start-ups. Shadow Chancellor Rachel Reeves has refused to rule out forcing pension funds to invest in a proposed 'future growth fund'. In a recent paper, the Tony Blair Institute reports that overseas investors currently invest much more in UK venture capital than UK pension funds do, and backs the idea of turning the Pension Protection Fund into a 'global-scale' scheme to invest in the UK economy.

This could raise fears that superfunds are a pretext for raiding people's pension assets so government can put them to 'good use'. If so, savers and trustees will be understandably hesitant. The question is whether superfunds would be used to apply short-term patch-ups to the economy, or for the kind of long-term investment that genuinely transforms our economy while also generating sustainable returns. We also need to be mindful of the realities of investing in illiquid assets. Venture capital, for example, is very high risk. A pension fund would need to invest consistently in the top 20% of funds in order to achieve superior returns, with the ever-present possibility of significant losses.

A more comprehensively new version of a similar idea is the 'collective defined contribution' (CDC) schemes introduced by the Pension Schemes Act 2021. This effectively constitutes a third type of scheme in addition to DB and DC. CDC schemes provide a 'target' pension like a DB scheme, but this can then be decreased (or increased) depending on the fund's performance. While just one CDC scheme has currently been authorised in the UK – the Royal Mail Collective Pension Plan – similar schemes are already operating in Denmark, the Netherlands and Canada.

Since CDC schemes effectively pool members' pension pots, savers have less say over investment choices, but in theory this should be more than compensated for by better returns. Most savers do not particularly want to be involved in day-to-day investment decisions, as long as they are confident their scheme is being run for their own benefit.

CDC could turn out to be the best of both worlds. There is no going back to traditional DB, but the great benefit of CDC is that it enables members to pool their risk without the funding risks to employers. If it can also provide much needed investment for UK infrastructure, so much the better. The real test of its success, however, will be winning the confidence and support of Generation DC.

Feature Article

A new agepathy: to adopt a retiree

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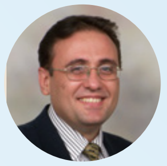

According to the Humane Society of the United States, around 3.2 million cats and dogs are adopted from shelters every year. There are no world statistics about adopted retirees.

There is a myriad of legislative solutions on pensions throughout the world. All of them are aimed at protecting the elderly by isolating specific measures and rules for them. And not surprisingly the elderly feel isolated from the rest of the society. "Old age", "Retirement", "Inactivity" etc. are becoming labels of pensiolation, i.e., isolation by legislation due to a current or expected retirement protection. Some recent estimates suggest that as many as 33 per cent of the world's adults consider themselves to be lonely. It is also reported that in 20 OECD countries, older people are more likely to be income poor than the total population.

By the way, the elderly used to be young themselves, although some might have forgotten it.

The somewhat careless and adventurous path of youth usually starts with apparent apathy to the boring and seemingly distant issue of age. Then, in adulthood it evolves quite soon into a sympathy with the elderly until empathy comes when the former young are already part of the evolving old-age crisis themselves. How about changing this traditional agepathy, which keeps repeating every 40 years or so for each new age cohort of people, starting at 20?

Some pension experts have spent all their professional lives in advising and consulting for that change to happen. However, rejuvenating the Social Security systems of the 20th century today seems to go far beyond the usual new layers of make-up, as those systems are close to retirement themselves, and new make-up would only make things worse. In view of the current wealth of world crises, it is quite inadequate to predict PAYG adequacy based on such seemingly certain former enabling factors as increasing birth rates, employment and salary which served as its constituent foundation in the past. Private funded systems are under great pressure as well from downward capital markets.

In times of demographic, economic and financial crises the long and acute rivalry between traditional PAYG and funded pillar solutions is becoming obsolete. Is a common and pillar-neutral backup to the traditional approaches thinkable? If not, think of the unthinkable. It is what mankind learned from the pandemic when reasoning and conventional logic stopped working overnight in almost all spheres of human life. One could only hope that the backup solutions mankind would think out would be humane because, by definition, humans are humane. But are humans humane to humans?

According to the Humane Society of the United States, around 3.2 million cats and dogs are adopted from shelters every year. More than 2/3 of US households share their homes with cats and dogs. 186 million cats and dogs live in 86 million households. Compared to the 1970s, pet ownership in America has increased by more than 300%. It is estimated that people have spent $99 billion on their pets in 2020. There are no world statistics about adopted retirees.

Imagine a world where you could adopt a retiree and be rewarded for your decision by the government via income tax incentives, e. g. lowering or waiving your social security tax in proportion to the partial or full financial support provided by you as adopter / adopters to the adopted retiree. Thus, a retiree will be bailed out of the respective Social Security system, be it partially, temporarily or for good. Current government expenses to adopted retirees would be lowered. Families adopting retirees would have much more disposable income. Although money would be paid directly to a retiree, it keeps its retirement purpose, and would keep on counting for the contributors' future PAYG retirement. Adopted retirees would not feel socially isolated. They may become active again in helping with sharing life experience, knowledge, and even caring for adopters' children (incl. for young adopters themselves).

In brief, instead of using the established institutional PAYG transmission, what would have been paid via social security taxes by working people to an anonimous retiree, could now go directly from the working adopter/adopters to the adopted retiree (partially, temporarily or for good). The traditional PAYG would become more direct and personalised. It is a question of a fine-tuned calculation on how much the tax incentive could be in proportion to the bailing-out of the Social Security system so that the latter should keep the balance between the lowered income and the lowered expenses.

Old-age poverty is not the only reason for retiree adoption. Not all retirees are necessarily poor. Some of them may also need to be adopted as members of a family and / or a labour active community for reasons other than the lack of financial resources.

Private funded solutions are not affected by such a PAYG deinstitutionalisation move and will preserve their relevance for retirement income adequacy.

Before one quickly labels all this as unthinkable, let us go back to the famous observation made by the CEO of Digital Equipment Corporation in 1977 when his engineers presented the PC prototype to him: "There is no reason for any individual to have a computer in his home."

A Social Security reform is not always a question of getting more money in. It is rather a question of getting more value too. And the value of money is a good reason to think of having PC (Pension Care) at home.

Feature Article

DB Scheme Funding: Some Empirical Results and Considerations

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Con Keating
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We have been collecting the reported funding ratios of DB schemes since December 2022. Through this analysis we are finding some fairly large discrepancies between reported funding ratios and the widely broadcast narrative of highly significant improvements of those ratios across the sector. One basic figure from our analysis is that the range of funding ratios spans 50% to 161%.

In this note, we touch upon some of the notable points of our collected sample of 350 schemes. Of course, at slightly less than 7% of the universe of private sector-funded DB schemes, this sample is not large enough, nor sufficiently assured of being representative, to prove or disprove anything, but it is sufficiently large to raise questions and concerns.

First, there is no scheme in this sample which reported a positive return on assets in 2022. The best three reported results are losses of 3.8%, 4.6%, and 5.1%; the worst performances show losses in excess of 40%. This means that any improvements in funding ratios must have been derived solely from declines in the present value of scheme liabilities.

Second, 32% of our sample saw their funding ratios deteriorate over the year. The median deterioration was 4.1%. There is a pronounced difference in the symmetry of the distribution of improvements/deterioration. The median improvement was 11.6%. The median funding level of our overall sample was 95.4% in December 2021, and this improves to just 102.1% by the end of December 2022.

It is also evident from the sample that schemes which were in deficit in 2021 were far more prone to experience deteriorations in the 2022 funding ratios than schemes that were in surplus, which exhibited a tendency to improve further.

Before illustrating why this should be the case in Box 1 below, it is worth considering how much the returns of funds might be expected to have been. With the gain due to the decline in the present value of liabilities for schemes overall estimated by the PPF to be 38.8%, hedging 50% of interest rate exposure would suggest a gain from this of 19.4%.

With , say, 50% of the fund invested in other growth assets which lost, say, 10%, we would have expected our sample to return 14.4% (19.4% – 0.5*10%)[1]. Our results are consistent in terms of both the overall results (6.7% gain), and the gain (11.6%) and loss (4.1%) partitions, when the allocation of those schemes to growth assets was 44% and schemes were overall 72% hedged.

This can also serve as a sense check for the claims of 15% or more overall improvement in scheme funding. This would have required LDI hedging of only 49%, far below its level by most accounts and in our sample.

We would also note that with the presence of the present value of liabilities in the denominator of the funding ratio, the ratio may improve even though the amount of surplus funds has fallen. A constant cash surplus of say £10 and a funding ratio of 110% in 2021 with liabilities at £100, would be reported as an improvement to 16.34% in 2022, if the liabilities have declined to £61.2% (this is assuming a 38.8% decline as reported by PPF for the market overall).

The best three improvements in the sample were from 58% to 90%, from 68% to 104% and from 88% to 137%. These improvements, to schemes that were in deficit, are all of schemes which were not employing LDI or doing so only to a very limited extent and without leverage. The worst deteriorations were from 97% to 74%, from 88% to 69% and from 83% to 65%. The largest gain in funding ratio was 55.2% and the greatest loss, 23.2%.

41.5% of our sample were in deficit on their section 179 value at December 2021, which agrees closely with the PPF's overall estimate of 41.3% at that date. However, the PPF's estimate that, at December 2022, just 13.4% of schemes were in deficit disagrees significantly from our sample estimate of 22%.

Feature Article

Box 1. Illustration of the LDI problem for schemes in deficit

The table below shows a notional scheme in deficit which has assets of £80 and liabilities of £100; it was at end 2021, 80% funded. If we assume the scheme adopted an LDI strategy which perfectly (and without any costs) hedges the interest rate sensitivity of the liabilities. In 2022, this LDI strategy results in a loss on the hedge of £34, the amount by which liabilities have declined (from £100 to £66)

	2021	2022	Return
Scheme with deficit			
Assets	80	46	-42.5%
Liabilities	100	66	-34.0%
Funding	80.0%	69.7%	
Fully funded scheme			
Assets	100	66	-34.0%
Liabilities	100	66	-34.0%
Funding	100%	100%	

The result is that assets decline by £34 from £80 to £46. The liabilities have declined by 34% but the assets have declined by 42.5%. The funding ratio of this notional scheme declines from 80% to 69.7%. This provides a direct challenge to the wisdom of fully hedging the interest rate sensitivity of liabilities when schemes are in deficit.

To quote one of our correspondents:

"For most of these (schemes with low or inadequate asset coverage of liabilities) TPR has encouraged an overtly defensive attitude, getting them to double up on their LDI positions "to protect the coverage you have as the first objective" – all part of TPR's real objective which is to minimise calls on the PPF."

With TPR pushing schemes in this direction, this approach has been actively promoted by consultants and advisors.

The scheme in balance shows no gains in funding ratio. Of course, a scheme in surplus, say 150% funded, will show a gain from 150% to 176% even though its assets have fallen from £150 to £116. The decline in the present value of liabilities, the denominator of the funding ratio, drives this increase.

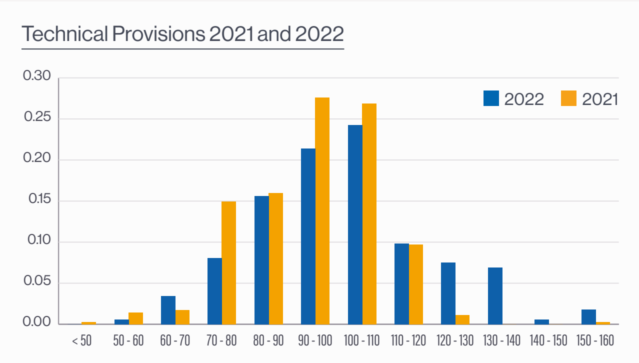
It is worth highlighting explicitly the implications of this. Full hedging will tend to decrease funding ratios for schemes in deficit and increase them for schemes in surplus, when rates rise, and the present values of liabilities fall. We should expect the net overall improvement or decline in the funding ratio to be determined in part by the ex-ante distribution of scheme funding. Just 30.6% of the schemes in our sample were in surplus at the end of 2021. The second major effect on the distribution of outcomes is of course the distribution of LDI hedging levels, and their costs.

While we have focussed on the 2021-2022 year, a period of interest rate rises and liability declines, this differential action is present also in other years when interest rates were declining and liabilities rising. In times of declining interest rates, the differential action will tend to compress the range of outcomes rather than expand them as is seen with interest rate increases.

Conversely, this differential action in times of rate increases will increase the dispersion of resultant funding ratios for the overall funded DB system making it intrinsically riskier than would otherwise be the case. Adding leverage to the LDI strategy compounds and increases this dispersion or riskiness further. In our sample, this increase in dispersion is substantial. When measured as the first moment of the distribution about its median, it is a threefold increase. It is evident visually in Figure 1, the comparison of the sample distributions for 2021 and 2022.

Figure 1 below shows the funding ratio distributions of our sample at December 31st 2021 and December 31st 2022. The observation that there were both gains and losses is evident from this Figure. For example, the increase in 2022 of schemes funded between 60% and 70% can only be explained by more schemes experiencing declines in scheme funding than from improvements in funding, as the number of schemes in this range in 2022 is greater than the total number of schemes combined in the 50-60% and less than 50% range in 2021.

Figure 1: Distribution of Funding Ratios, 2021 and 2022



The most pronounced improvements are of schemes which are now 120% or more funded. However, this is a modest proportion of our sample, 16.8%, which is an increase of 15.2% from the 2021 distribution. However, if we take 120% funding as the level needed for buy-out, it suggests that the Pensions Regulator's recent statement that 25% of schemes are now sufficiently funded to buy-out may be an overstatement.

Before moving to comparisons of our sample distributions with those published by the PPF, we shall consider two specific schemes within our sample – Table 1

Table 1: Scheme-specific examples

	2021	2022	Return
Scheme One			
Assets	83	43.55	-47.5%
Liabilities	100	65	-35.0%
Funding	83%	67%	
Scheme Two			
Assets	95	46.58	-51.0%
Liabilities	100	62.1	-37.9%
Funding	95%	75%	

Scheme One

Scheme One was 83% funded at the beginning of 2022. It reported scheme assets of £43.55 at the end of 2022. As the scheme was targeting 100% hedging, the decline in assets is attributed as to £35 to its LDI hedge and £4.45 to declines in the prices of other assets held. The scheme reports a funding ratio of 67% overall, which would have been 73.8% in the absence of those other losses.

Scheme Two

The funding ratio of this scheme was 95% at the end of 2021, very close to the median of the sample. Its liabilities dropped by 37.9% due to the rise in the discount rate from increased interest rates, to £62.10. The scheme reported assets of £46.58 at the end of 2022, down 51% from the £95 value reported in 2021.

This scheme was pursuing a strategy of using LDI not just to immunise against funding ratio declines but also to repair deficits. This strategy was widely promoted by advisors and consultants, and apparently approved by TPR. It was targeting a 125% hedge of liability movements. The loss of £48.43 can be attributed to LDI as to £47.38 and £1.05 growth assets (-2.56% on the amount invested).

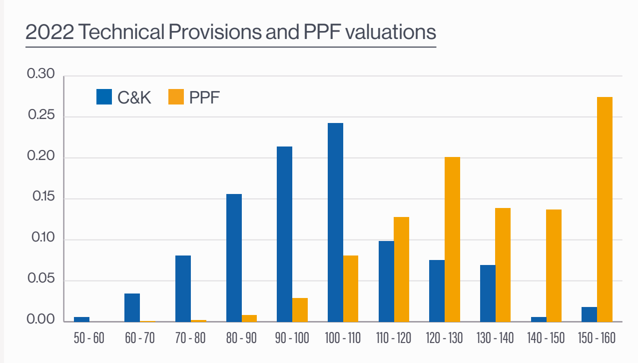
This strategy of leveraging the portfolio flies in the face of the old market adage: "The road to hell is paved with the carry trade." The decline in scheme assets of 51% left the scheme just 75% funded at the end of 2022.

Losses on LDI, liability declines, and the distribution of outcomes

There are many schemes reporting losses on their LDI portfolios far in excess of the decline in the present value of scheme liabilities. For some, it was the result of deliberate over-hedging as in the case of scheme Two above. However, for many it was the product of financial incompetence as they were targeting 100% hedges which proved different in practice. This error most commonly arises from the use of the mathematical modified duration for Index Linked Gilts and corporate bonds when their empirical volatility is far higher than that. In the case of Linkers, this volatility stems in large part from the concentrated nature of the holdings by pension funds, and in the case of corporate bonds, from the failure to recognise that part of the yield spread is compensation for default and credit migration, and that the yield spread has a life of its own.[2]

Figure 2 below compares the PPF 7800 published distribution of funding levels and that of our sample (C&K) at December 2022.

Figure 2: PPF 7800 funding levels and C&K funding levels



It is evident by inspection as well as formal statistical tests that these distributions are dissimilar. This is of course a comparison of two different valuation bases, the PPF section 179 value and scheme technical provisions. The principal source of idiosyncratic differences in these two valuation bases is the degree of maturity of schemes, that is the relative proportions of pensioner and deferred member claims. However, if we consider this difference to be broadly similar across schemes in our sample, say 20% in funding ratio, we may simply transpose our distribution as is illustrated in Figure 3 below.

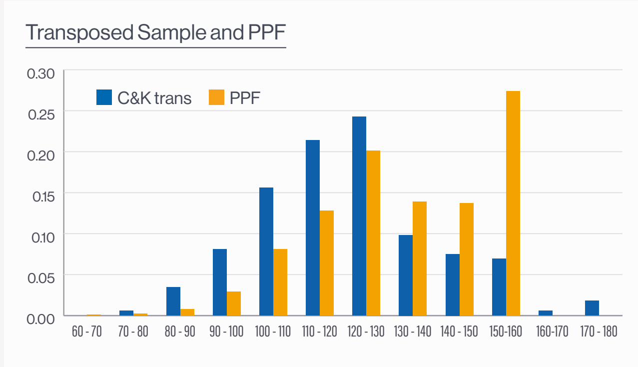


Figure 3: Transposed (+ 20%) sample and PPF distribution of funding ratios

The transposition of the sample, of 20%, is we believe somewhat higher than the true difference between scheme technical provisions and will tend to inflate the number of schemes apparently able to buy-out. Given the maturity of schemes, that is the relative proportions of pensioners and deferreds and the structure of PPF compensation arrangements, we would estimate a more accurate transposition would 15%.

Feature Article

If we consider 130% funding on a PPF basis to be the level of funding needed for buy-out, 55% of schemes would, by PPF reckoning, be able to buy-out. If we were to consider 140% to be a better guide to the buy-out level this falls to 41%. These are respectively 28% and 24% above our sample estimates. Indeed, if we consider the correct transposition to be the more conservative 15% rather than the more generous 20% of Figure 3, then 21.7% of sample schemes are expected to exceed the 130% funding level and 13.1% to exceed the 140% level. The PPF estimates are two and threefold multiples of these values.

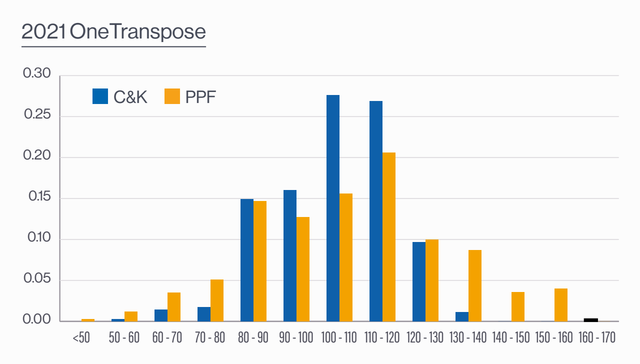
We can also consider the end 2021 results reported by PPF as a possible mechanism for calibration of the difference between their s179 value and the sample TP median funding ratio. The 2021 PPF 107.7% funding is equivalent to the 95.4% of the sample data, an adjustment of 12.3%. If this differential were applied to the sample 2022 results, 102.1% technical provision funding becomes 114.4% as a PPF equivalent and that differs materially from the 136.5% reported by the PPF.

Examination of the PPF distribution and our sample as at the end of 2021 is also informative. For completeness, we should point out that the PPF distribution is marginally larger in 2021 than in 2022, whereas ours has a constant membership. For ease of examination, we show as Figure 4, the PPF distribution and our sample transposed by one bucket, 10%.

The PPF distribution had, at a 130% threshold, 16% of its schemes eligible for buy-out and at 140%, this falls to 8%. These are large numbers of schemes, 820 and 410 respectively. This prompts an immediate question: if this many schemes were eligible for buy-out in 2021, why did we not see far more than we did?

By contrast, our sample had at 140% PPF equivalent just 1.4% of schemes eligible and at 130% equivalent, this rises to 11% of schemes being eligible. At a 15% transposition as previously discussed, these fall to less than 1% at 140% and to 6% at the 130% threshold, that is from 600 schemes as the PPF number to around 50 schemes based on our data.

Figure 4: Distributions of funding ratios for PPF and the sample, transposed by 10%.



The empirical analysis we have conducted strongly suggests that, if our sample is representative of the overall universe of schemes, funding ratios have not improved by as much as is widely asserted. In particular, the improvement at higher funding levels is much lower than otherwise believed, for example, by the Pensions Regulator.

When combined with the upswell in discussions of schemes running on and off in self-sufficiency, it seems that the much publicised, and cautioned against, gold-rush bonanza of buy-out may be a rather muted affair.

LDI 2.0 and liquidity buffers

It is evident from their statements and actions that TPR would like to see a continuation of the use of LDI by schemes. This is evident in, for example, the formulation of larger liquidity buffers. It is notable that these buffers will operate in a manner counter to the carry-trade spread if they are to be maintained in cash as the pensions minister, Laura Trott has indicated:

"The framework expects that funds have sufficient resilience to respond to moves in the gilt market of 250 basis points at minimum, without the need to sell assets."[3]

The principal concern has been the avoidance of a repeat of the gilt market turmoil. We find this emphasis surprising for reasons which will become clear if we apply a simple stress test to schemes. The stress test we would apply is a repeat of the losses seen in 2022. By virtue of having occurred once it is plausible, if unlikely. We show first, as Table 2 below, the effect of such a shock on the illustrative scheme considered in Box 1.

Table 2: 2022 as a stress test of our hypothetical scheme.

	2022	2022 Stress test	Return
Assets	46	12	-73.90%
Liabilities	66	32	-51.50%
Funding	69.70%	37.50%	

The effect is obvious, the same magnitude of shock as previously produces a far larger deterioration of the funding ratio than was seen in 2022, 32.2% versus 10.3%. If we examine the two schemes considered earlier, the effect is even more pronounced, Table 3.

Table 3: 2022 as a stress test of our actual schemes

	2022	2022 Stress test	Return
Scheme One			
Assets	43.55	8.55	-80.4%
Liabilities	65	32	-51.50%
Funding	67.0%	28.5%	
Scheme Two			
Assets	46.58	8.68	-81.4%
Liabilities	62.1	24.2	-61.0%
Funding	75.0%	35.8%	

With these levels of funding, there is simply no way in which a scheme could recover without massive additional contributions from the employer sponsor; fixed costs and pensions payments which might conservatively be of the order of £3 per annum would make additional support from the employer a necessity.

These schemes are on the verge of bankruptcy. The stress is catastrophic in effect. Schemes which have failed and entered the PPF have done so because of the insolvency of their sponsors rather than the scheme itself. The principal point here is that TPR ought not to favour LDI for these schemes in deficit and already reduced circumstances. In doing so, it is increasing the likelihood of major losses for the Pension Protection Fund (PPF), which can scarcely be considered protecting it, one of its statutory objectives. Of course, schemes which are well funded do not benefit the PPF. Indeed, because of these differential effects, TPR should never have supported and advocated the use of LDI and leveraged LDI.

In this note we have considered the funding ratio as a measure of scheme sufficiency. This is the most widely used metric in practice. We would actually prefer another more intuitive metric, schemes assets as a proportion of undiscounted projected liabilities. With this measure, declines in asset values or increases in projected liabilities will be reported as decreases in coverage.

Final thoughts

While most of this commentary has been concerned with the effects of LDI on asset values and the funding ratio, there are also to be material differences in the changes to the present value of liabilities. The PPF reports liabilities having declined by 38.8% over the year to December 2022. For comparison, a 15-year duration discount function would have declined by 34% and a 20-year by 42.7%. Our sample shows very considerable heterogeneity with liability declines from as little as 7% and 8% to as much as 41% and 42%. However, the vast majority of our sample are clustered between 30% and 35%. Of course, changes to inflation and mortality assumptions will affect liability estimates, but these observed differences still appear to be very large by comparison with plausible estimates of those potential effects taken account of.

Last, and most importantly, it is easy to overlook the significance of a ratio difference. A difference of 20% in the overall funding ratio of DB schemes is a difference of the order of magnitude £200 billion to £250 billion in monetary terms. This is no small beer and given the sensitivities of ratios, very small changes will lead to very large changes in the perceived overall position of funding.

[1] In these calculations, we are abstracting from the surplus/deficit issues discussed in Box 1. As the sample median was 95.4% funded, we do not believe this introduces a major bias into the calculations which follow.

[2] In this analysis of these two schemes, the costs of realisation of liquidity during the Gilts crisis and the subsequent rebalancing of portfolios, which appears still to be ongoing, are attributed to the residual non-LDI assets, as these costs are not currently separable in published or other data.

[3] https://committees.parliament.uk/publications/39828/documents/193805/default/

EPMI Column

Belonging in the Pensions industry

Sarah Brennan
Professional Trustee, Dalriada Trustees limited

I started my very first pensions job in 2003, at a time where schools were only interested in you if you wanted to go University. That wasn't for me. I wanted to get stuck in, learn and find my own feet. Admittedly, I didn't know I was getting in to pensions, but I'm still here 20 years later and feel passionately about making our industry even more diverse, making people feel like they belong, and making life that bit fairer.

I'm a professional trustee, have been for over 10 years, and worked in pensions administration for 10 years prior to that – a very undervalued part of our industry which offers so much learning for everyone, and of course, are the people dealing with our members.

You've probably heard of imposter syndrome - there have been, and still are times when I doubt myself, I know of others that feel the same. Often the perceived pressure to know everything, especially as a professional trustee, can be daunting. But no-one knows everything, and that's where the multitude of different expertise/experiences/ personalities in our industry shines through. Teamwork is so important, and for me, offers so much more than someone's technical ability.

I always, perhaps incorrectly, thought having a degree, or qualification, gave someone immediate credibility, which is challenging in an industry full of intelligent individuals, often with impressive academic backgrounds. I was really pleased that PMI brought out a membership that is based on experience and knowledge. I can happily say I'm a member of PMI by Experience, which might not sound a big deal, but it goes a long way in helping people like me feel like they belong in the pensions industry.

I'm really proud to actively sit on a few committees, such as NextGen Research and Insights Committee, The Pensions Equity Group and TPR's D&I committee, which are all focused on areas close to my own heart. I've met some fantastic individuals - shared stories, sought guidance, found allies, which is invaluable support and I think genuinely helps people from all walks of life get involved and feel like they belong.

I'm extremely honoured to have recently found out that I've been nominated in the Women in Pensions Awards for both trustee of the year and the Unsung Hero award. I had never imagined that I would be 'good' enough to be nominated for any award and wish my colleagues and nominees the best of luck.

EPMI Column

The journey continues

Paul Jayson
Head of Pension Executive & Management Services, Barnett Waddingham

I have always thought of myself as an unusual actuary – one who can't get too excited by detail but absolutely loves the power of communication. I get a real buzz out of untangling complex problems and suggesting practical ways to achieve clients' objectives through creative thinking.

Luckily Barnett Waddingham has supported me in carrying out other roles alongside my actuarial work - providing me with a well-rounded, interesting and challenging career. I have supported colleagues with their commercial relationships, led our business development team and managed some of our biggest and most important client relationships. Now my varied career has taken a new turn, and as head of our Pension Executive and Management Services business I am able to use everything that I have learnt before but in a less mathematically technical environment.

My new role (well, it's been a year now) enables me to bring all my interests and strengths together in one place:

- Providing support and guidance to clients in the critical area of pension scheme management and governance, enabling trustees and sponsors to achieve the best outcomes for members who rely on the schemes we look after for a good standard of living in retirement.
- Adopting a commercial approach to our service delivery so our clients get great value and a flexible, proactive and pragmatic service.
- Engendering a coaching culture in our team that not only empowers everyone to achieve their potential but also creates a fantastic team dynamic that fosters a culture of support, development and freedom to come up with new ideas.

Moving away from actuarial work hasn't meant I need to give up my membership of the actuarial profession and I'm proud to operate within their ethical and professional framework. It has, however, enabled me to join the PMI based on my experience in pensions. I'm really looking forward to taking part in their learning and development initiatives, as well as participating in their networking events as I develop in my new area of specialism. I have already taken part in several seminars and events and really enjoyed the passion that the PMI shows for supporting each other and our industry.

Looking ahead, efficient management of pension schemes and good governance are going to be ever more important to DB schemes as they approach their end goal - and to DC schemes as they increase in prominence to provide people with a good standard of living in retirement. It is incumbent on all pension professionals to facilitate this. I am excited about the evolution of our business as we rise to meet the challenges ahead by learning new skills (many of them rather softer skills than we might be used to!) and innovating the way we work (in this ever changing world we can't stand still!).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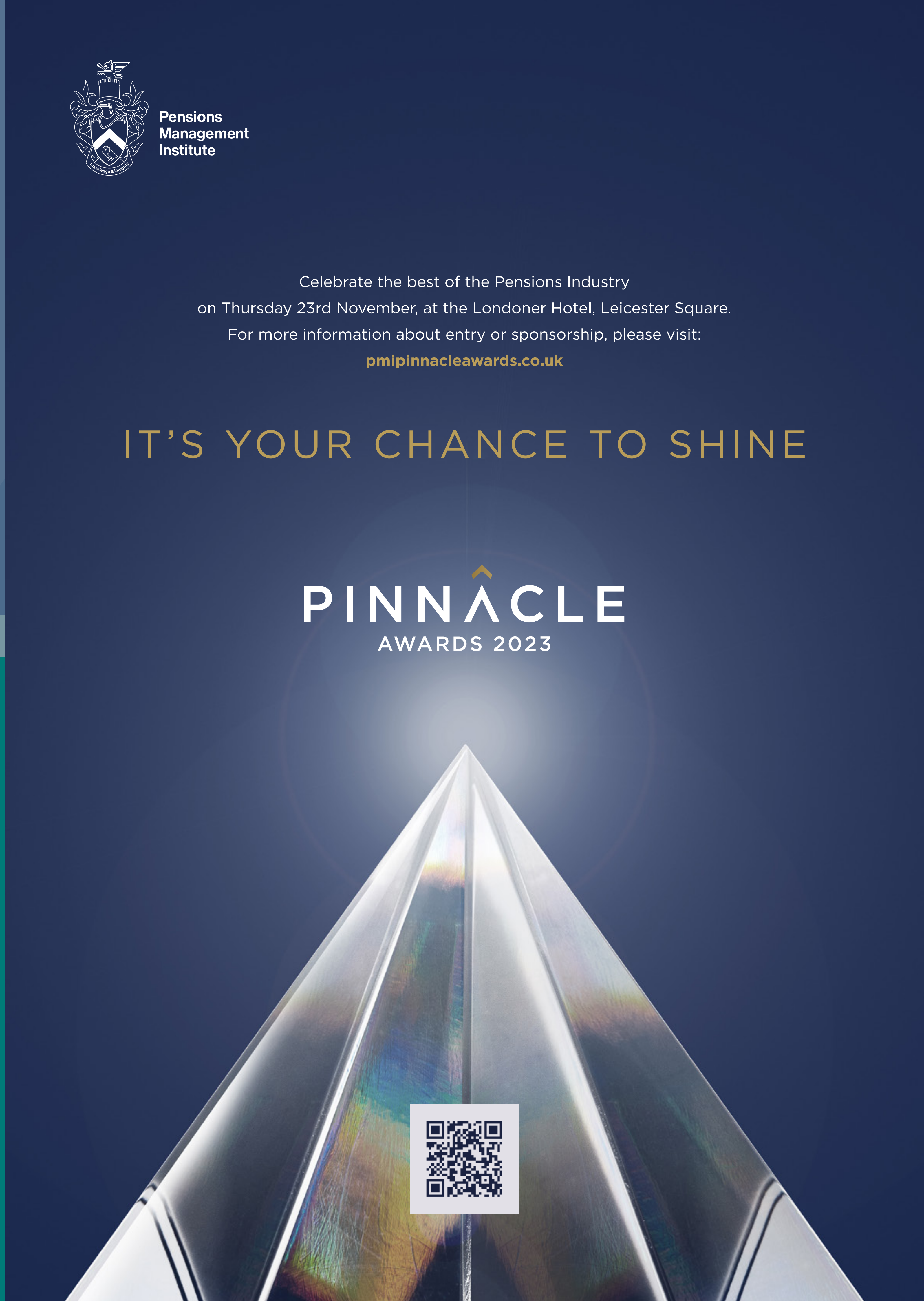
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AWARDS 2023

Pension Conundrum

Pension Conundrum

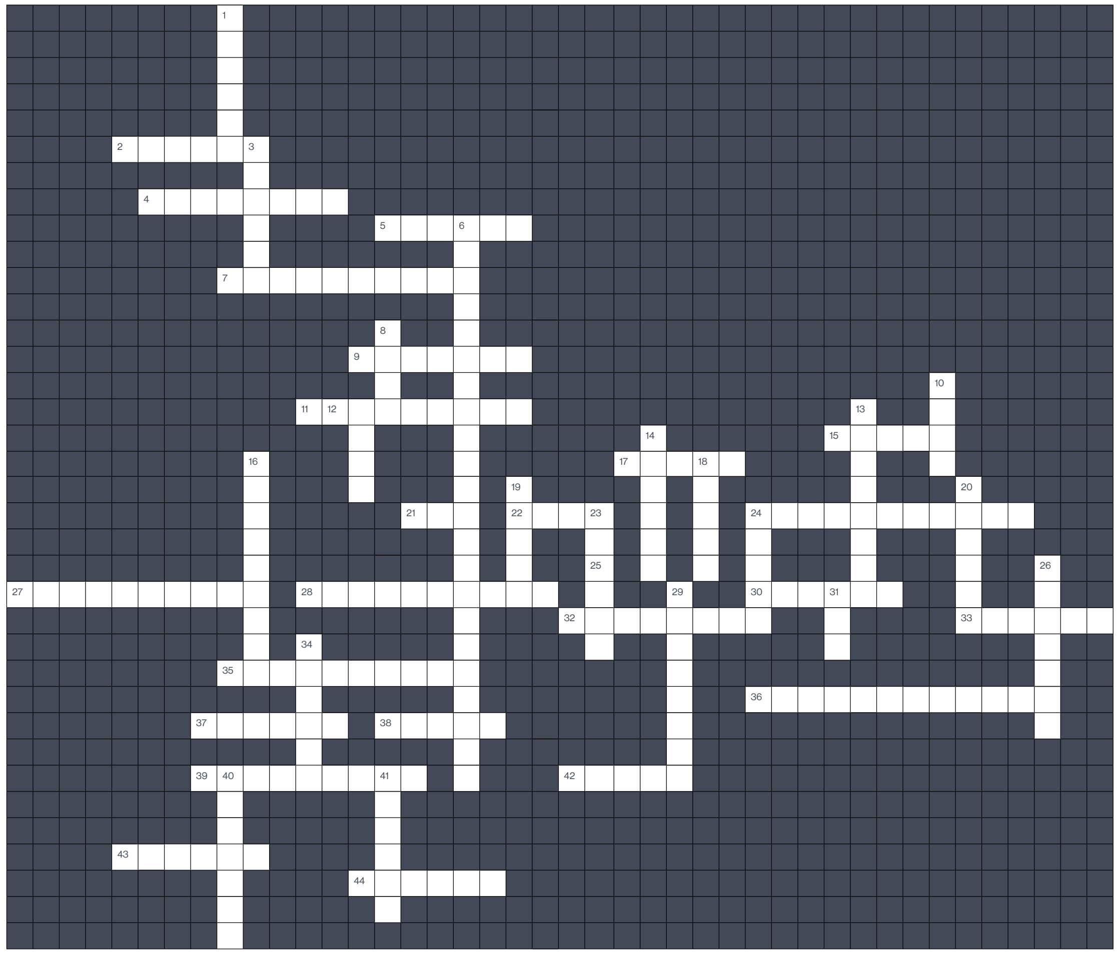
Crossword

Across

2. Resolution (6) **4.** Doing nothing (8) **5.** Benign, kind (6) **7.** Captured attention (10) **9.** Interests (7) **11.** Creation (9) **15.** Find explanation for (5) **17.** Take ownership of (5) **21.** Poor (3) **22.** Possess (4) **24.** Medium of visual art (11) **25.** Income (3) **27.** Uncertain (10) **28.** Operator (10) **30.** Period of years (6) **32.** Logical (8) **33.** Gap (6) **35.** The work of keeping financial records (10) **36.** Decline (12) **37.** Quantity (6) **38.** Unmanned flying vehicle (5) **39.** Criminal (9) **42.** Heartbeat (5) **43.** Supporting column (6) **44.** Largely (6)

Down

1. Crossing (6) **3.** Keep (7) **6.** Machine capable of learning (10,12)intelligence **8.** Show optimism (4) **10.** Fanatic, especially with regards to tech (4) **12.** Differ (4) **13.** Combine (8) **14.** Guidance (6) **16.** Convincing (9) **18.** Ordinary (5) **19.** Form (5) **20.** Wire rods (6) **23.** Present alternatively (6) **24.** Self-respect (5) **26.** At sea (7) **29.** Conversation (8) **31.** Time of life (3) **34.** Gen Z (6) **40.** Sympathetic reaction (7) **41.** Unjust (6)



Answers from Issue 49

Across

3. Educating **5.** Expansion **9.** Rally **12.** Remind **14.** People **15.** Risk tolerance **16.** Refinement **17.** Balance sheet **18.** Biodiversity **19.** Prudential **21.** Firm **26.** Commit **27.** Construct **29.** Transition **31.** Lunch **32.** Accrual **35.** Over time **38.** Testimonial **39.** Innovation **40.** Gold standard

Down

1. Portal **2.** Sensationalist **4.** Luxury **6.** Short termism **7.** Indebted **8.** Private credit **10.** Mitigate **11.** Classes **13.** Targeted **14.** Pie **15.** Robust **16.** Risk parity **20.** Impact **22.** Matching **23.** Lock **24.** Prior **25.** Tomorrow **28.** High level **30.** Slow down **33.** Co opt **34.** Ratings **36.** Spike **37.** Most **39.** Issue

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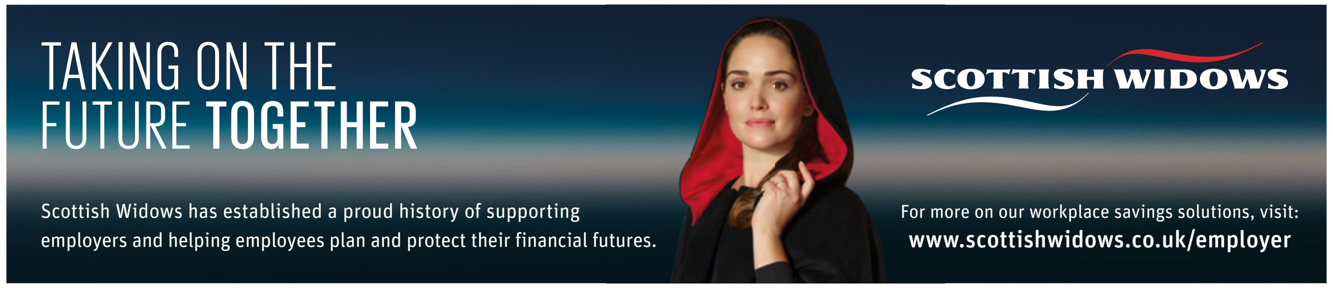

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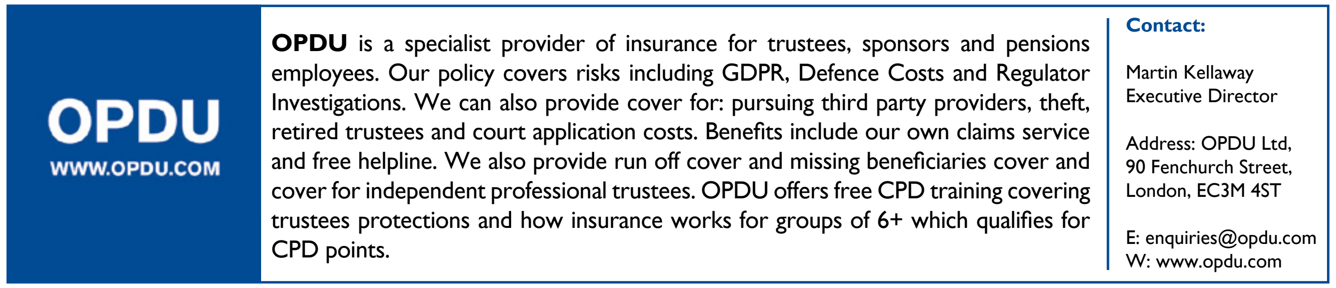

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