

# Pension Insurance Corporation

Pension Risk Transfer Index

Q2 2010



# Highlights



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## ■ Increased interest in risk transfer solutions has continued during Q2 2010, despite the considerable volatility in the asset markets

- ▶ Overall affordability impacted by the narrowing of long-dated real gilt yields and the significant equity market volatility
- ▶ Trustee boards are increasingly seeking full or indicative quotes
- ▶ Pensioners are able to be insured currently for marginal cost over the scheme's funding levels
- ▶ The 3% fall in the FTSE 100 on 29 June 2010 demonstrates the volatility in the markets, impacting pension funds

## ■ Trustees are seeking to bolster funding positions

- ▶ Wider use of contingent assets
- ▶ Possible use of these assets to finance future risk transfer transactions
- ▶ Heightened awareness around the weakness of the corporate covenant

## ■ Economic uncertainty will affect pension funds' funding levels and the risk transfer market

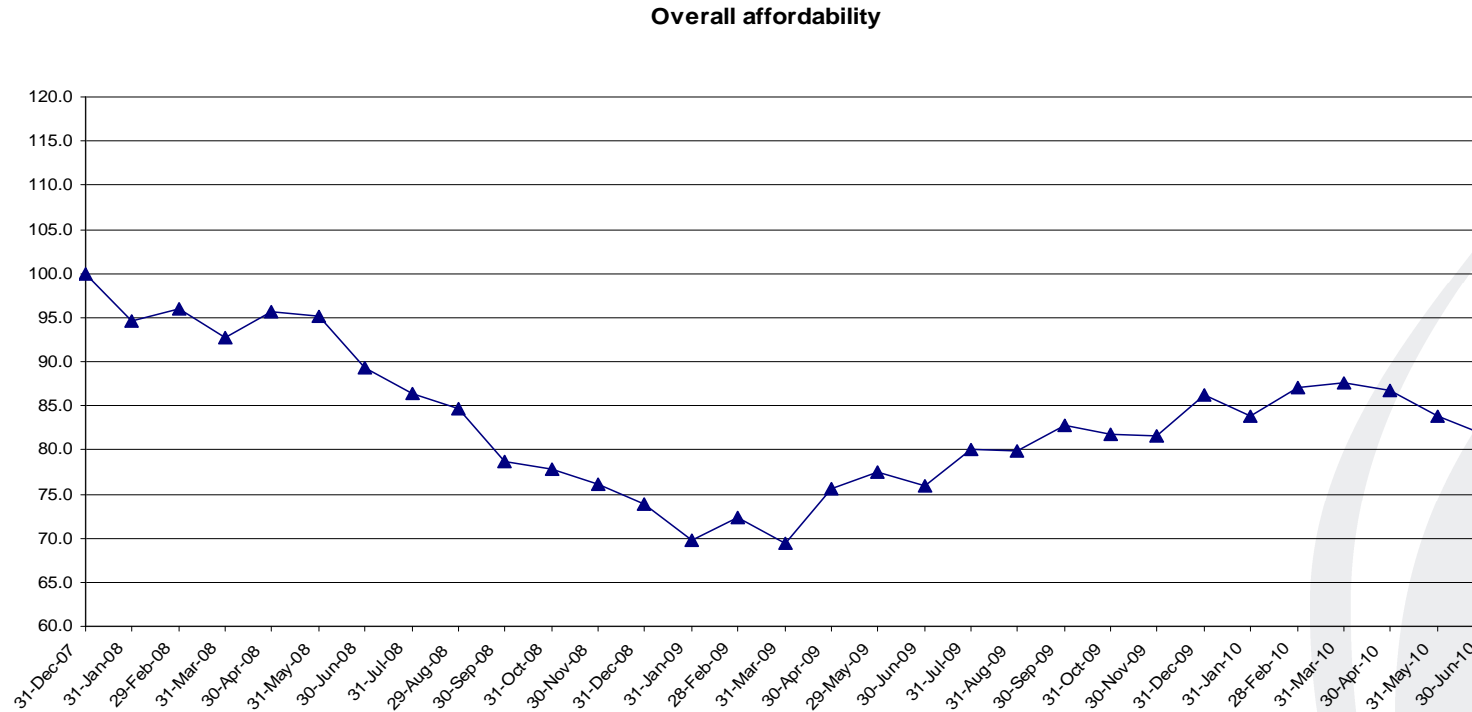
- ▶ Schemes which could have taken risk off the table earlier in the year, but missed the opportunity to do so, may have seen their deficits widening
- ▶ Possibility of a double dip recession and the impact of deflation on benefits is heightening Trustee concerns

# Pension Risk Transfer Index



# Overall affordability – scheme as a whole

The development of asset values expressed as a percentage of buyout cost



**Key:**

Chart shows 'overall affordability' for a scheme with a blend of deferred and pensioner liabilities, and invested in a 65% equities / 35% bonds mix. 'Affordability' considers the cost of insuring the pension risk compared to the value of the assets held by the scheme. A higher value in the index means that insurance is more affordable for pension schemes (insurance costs have fallen and / or asset values have risen)

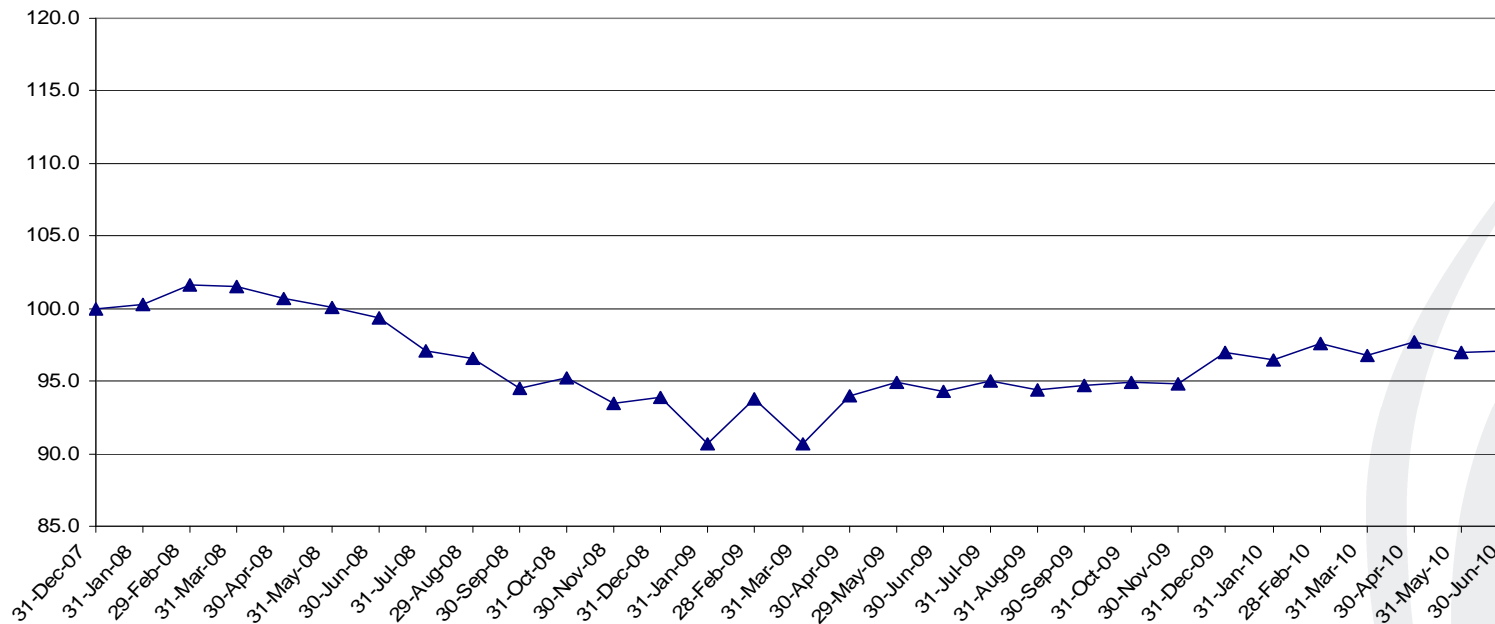
**Commentary:**

- ▶ Trustee boards are increasingly exploring their options with regard to risk transfer, seeking full or indicative quotes
- ▶ The double impact on pension fund deficits of the narrowing of long-dated real gilt yields and the significant equity market volatility has impacted overall affordability somewhat
- ▶ Schemes with significant equity holding are accepting that their funding position will remain volatile. They are assuming that this volatility can be supported by the sponsor – an assumption that will increasingly be challenged

# Overall affordability – pensioners only

The development of asset values expressed as a percentage of buyout cost

Overall affordability (pensioners only)



## Key:

Chart shows 'overall affordability' for a scheme with pensioner liabilities only and invested 100% in gilts and corporate bonds. 'Affordability' considers the cost of insuring the pension risk compared to the value of the assets held by the scheme. A higher value in the index means that insurance is more affordable for pension schemes (insurance costs have fallen and / or asset values have risen)

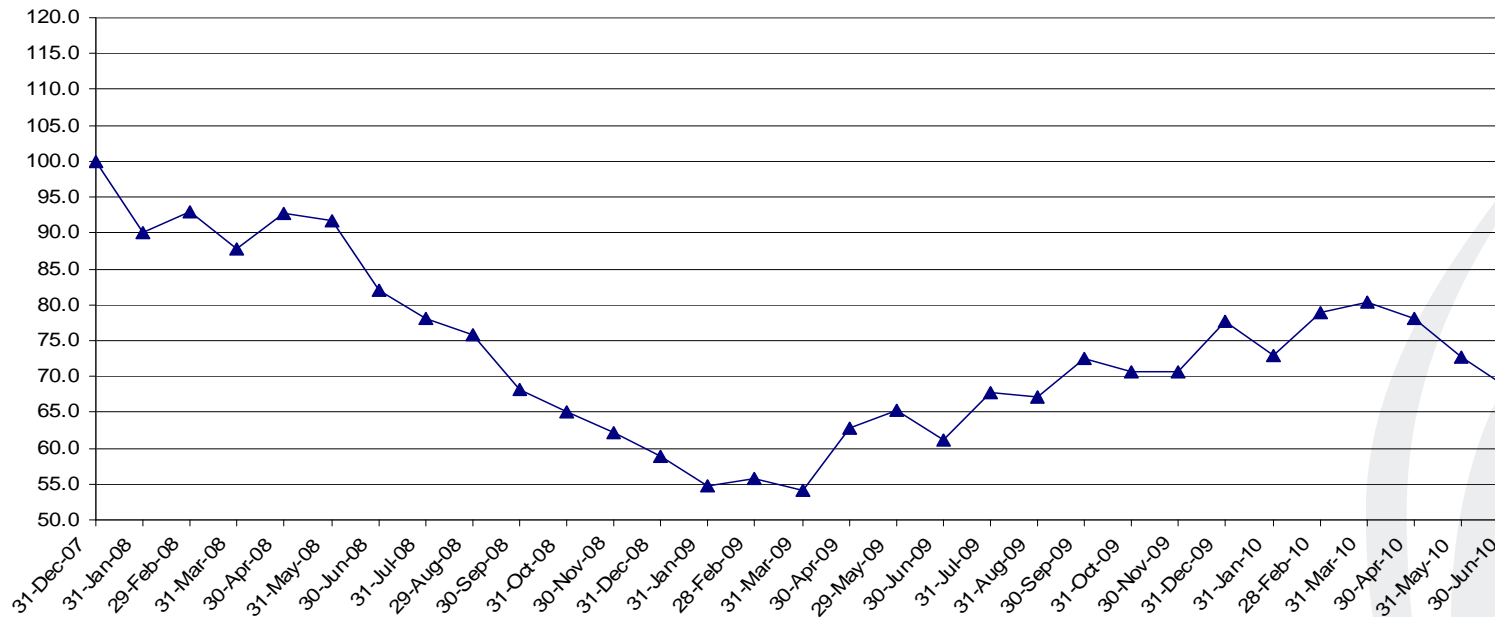
## Commentary:

- ▶ Levels of affordability for pensioners, who are often matched by gilt holdings, have continued to remain strong. Specific tranches of pensioners, such as the over 75's, can currently be insured for a marginal cost above the pension scheme's funding target.
- ▶ For schemes which are less well funded, but which have adopted prudent longevity assumptions, a partial longevity risk transfer solution can reduce risk at a low cost and be a step on the road towards full insurance

# Overall affordability – deferreds only

The development of asset values expressed as a percentage of buyout cost

Overall affordability (deferreds only)



## Key:

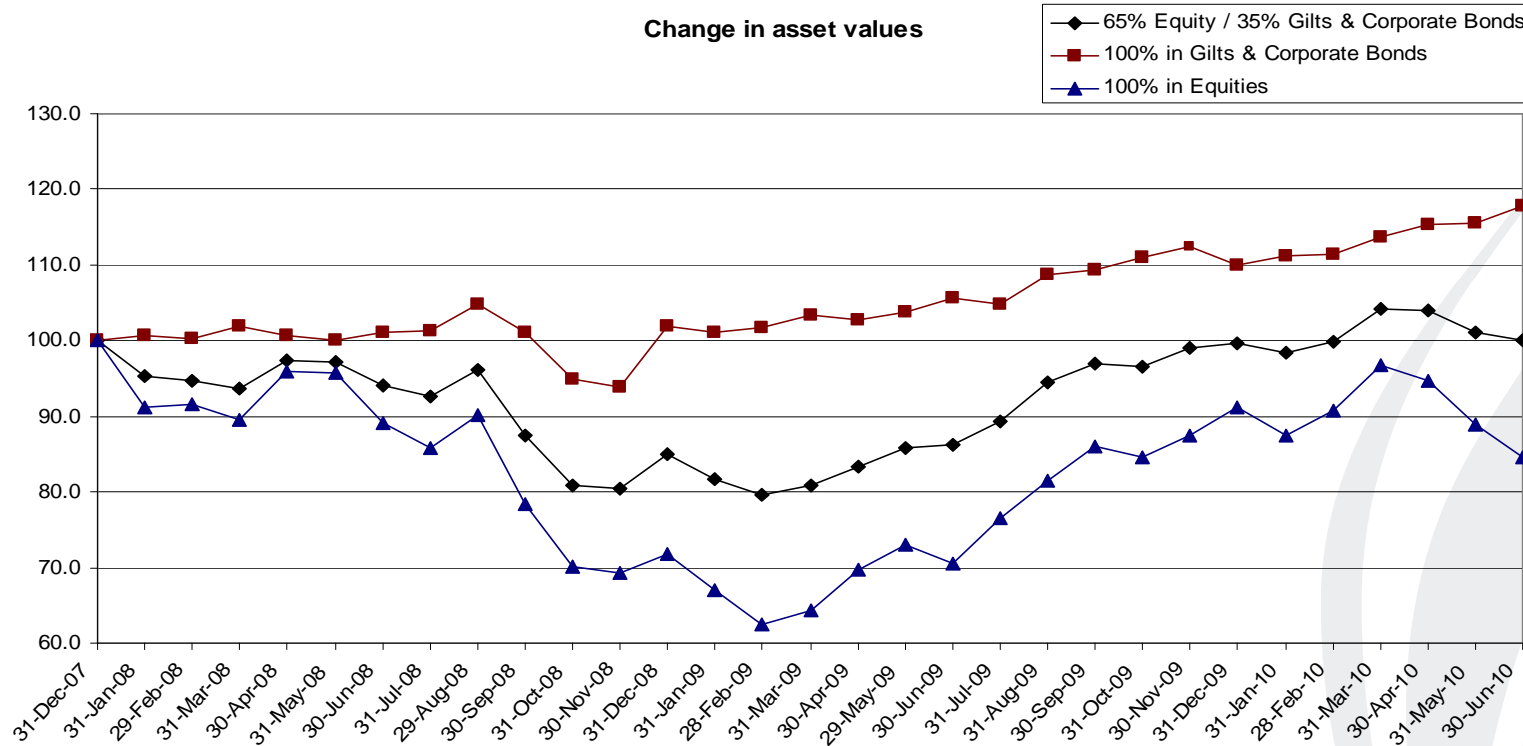
Chart shows 'overall affordability' for a scheme with deferred liabilities only and invested 100% in higher return-seeking investments, such as equities. 'Affordability' considers the cost of insuring the pension risk compared to the value of the assets held by the scheme. A higher value in the index means that insurance is more affordable for pension schemes (insurance costs have fallen and / or asset values have risen)

## Commentary:

- ▶ Affordability for deferreds has declined somewhat, due to the continued trend in long-term gilt yields and volatility in the equity markets
- ▶ Since the duration of deferred pensioner liabilities is longer than for pensioners, market volatility makes insurance pricing for deferreds fluctuate more than for pensioners

# Change in asset values

How the scheme asset values have moved in absolute terms – ie not relative to buyout costs



**Key:**

Chart shows relative movement in the value of a variety of investment strategies based on movements in common indices. ‘Gilts’ reflects a mix of Fixed Interest and Index-Linked gilts

**Commentary:**

- ▶ Volatility continues to remain high, especially in the equity markets. June 29 2010 saw a 3% fall in the FTSE 100 that could have seen almost £20million wiped off the assets of a £1 billion pension fund, assuming a 65% equity / 35% Gilts and Corporate Bonds mix
- ▶ High levels of uncertainty around the asset markets and economic situation continue to dominate trustee thinking, including around inflation / deflation and a double dip recession

# Disclaimer

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## About Pension Corporation

Pension Corporation is a leading provider of risk management solutions to the trustees and sponsors of defined benefit pension funds. It oversees pension fund liabilities of c.£7 billion and is affiliated to more than 100,000 pension scheme members or former members. Its FSA authorised and regulated insurance company, Pension Insurance Corporation ("PIC"), brings safety and security to scheme members' benefits through innovative, tailored solutions. These include pension insurance buyout or buy-in and longevity risk management. It has transacted both the UK's largest and the first public sector backed pension insurance buyouts. Other clients include FTSE 100 companies and several multinationals. PIC is proud to work with pension fund trustees to maximise member benefits. For further information please visit [www.pensioncorporation.com](http://www.pensioncorporation.com)

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