



The Pensions Trust  
Growth Plan  
30 September 2008 valuation results  
Employer Forum – 23 June 2009

**Actuaries and Consultants**

HSBC 

# Agenda

- Recap on valuation results at 30/9/05
- Market conditions at 30 September 2008
- Assumptions adopted for the valuation at 30 September 2008
- Results of the valuation
- What has happened since 30 September 2008 in financial markets
- Summary of key issues going forward

# Growth Plan – Liability recap

- Four types of liabilities:
  - Series 3 non pensioners – member investment accounts, backed by money market funds, increasing over time through new money and interest
  - Series 1, 2 and 3 pensioners – backed by annuities, increasing in numbers over time
  - Series 1 and 2 non pensioners (only Series 2 have increases in payment), backed by equity/property type investments, reducing in numbers over time
  - Future expenses

## The 2005 Valuation - results

	Technical Provisions basis	'Buy-out' basis
Assets £m	675.2	675.2
Liabilities £m	704.5	900.6
Funding level	96%	75%
Surplus/ (Deficit)	£(29.3)m	£(225.4)m

# Recap - 2005 Valuation results

- Technical Provisions projected to recover to 100% within 5 years, if:
  - investment returns and inflation in line with long term projections
  - interest rates unchanged
  - mortality projections unchanged (2008 study results will be important)
- Trustee decided to not seek additional employer contributions at this stage
- The Pensions Regulator accepted the Trustee's Recovery Plan

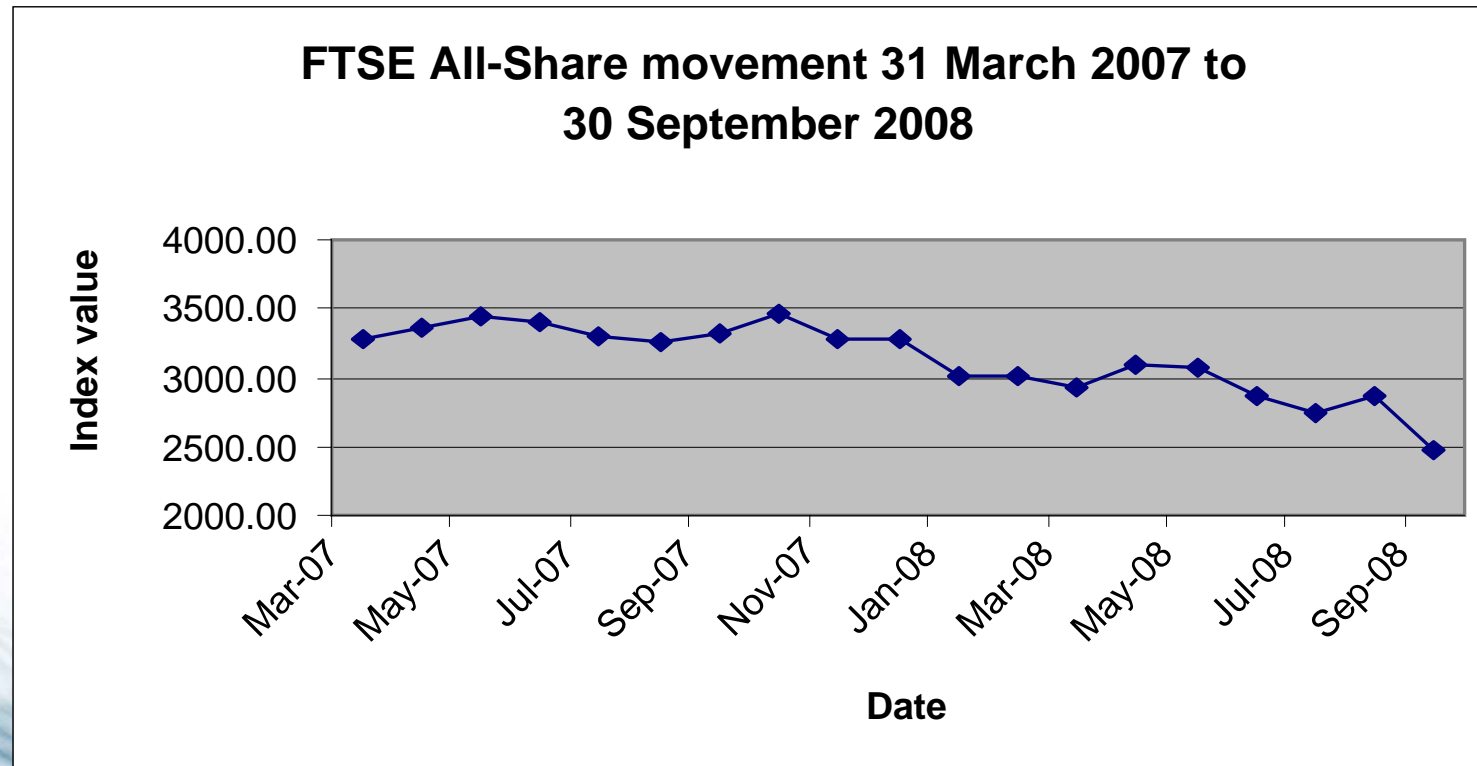
## Update at 31 March 2007 as presented at 2007 Forum

	Technical Provisions basis*		'Buy-out' basis*	
	Sept 2005	March 2007	Sept 2005	March 2007
Assets £m	675.2	782.4	675.2	782.4
Liabilities £m	704.5	729.5	900.4	899.9
Funding level	95%	107%	75%	87%
<b>Surplus/(Deficit)</b>	<b>£(29.3)m</b>	<b>£52.9m</b>	<b>£(225.4)m</b>	<b>£(117.5)m</b>

# August 2008 Pensioner Buy-in

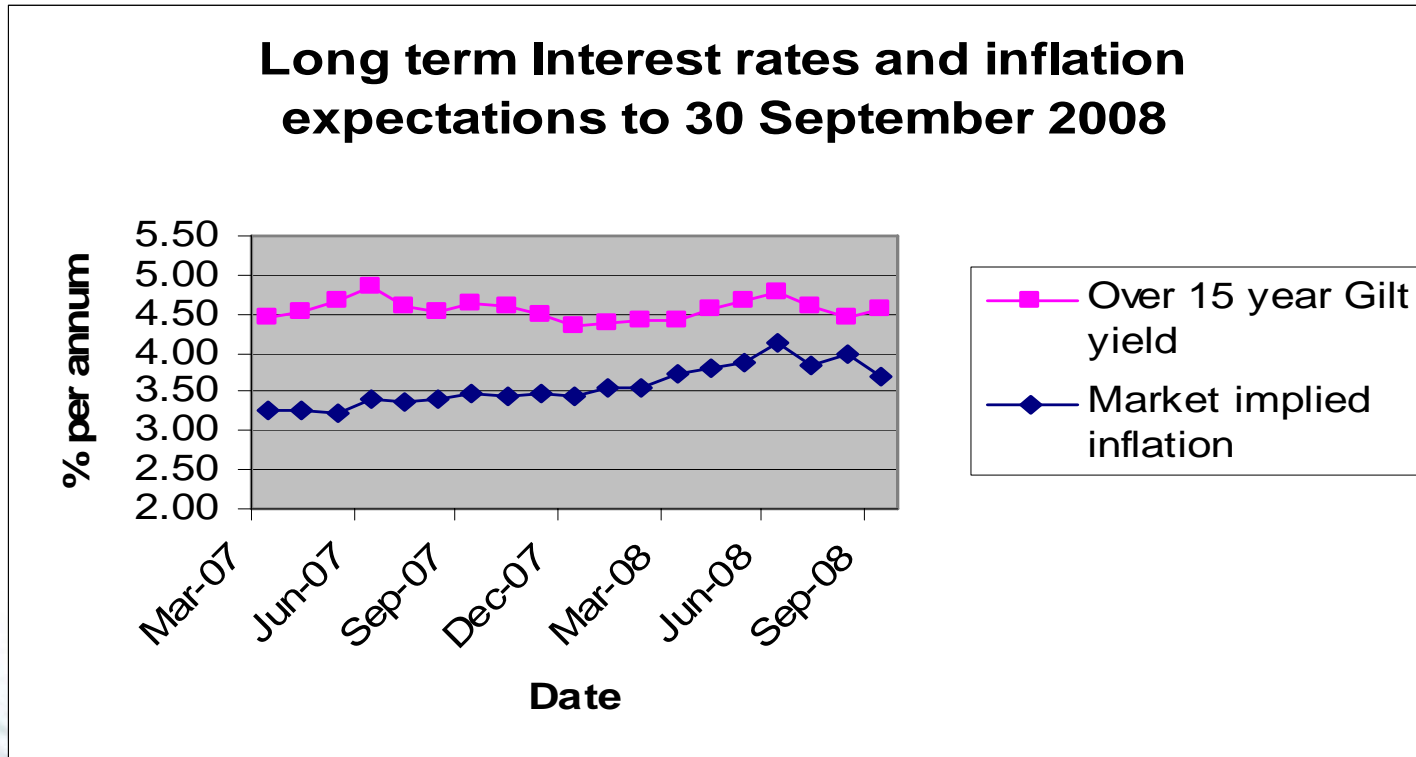
- Purchased annuities for current pensioners
- Paternoster chosen as insurer after detailed due diligence
- Effect is to transfer investment risk and longevity risk to the insurer, removing volatility on this part of the Plan's liabilities
- Pensioners remain members of the Plan, the Trustee simply now has an asset that matches the liability
- Equities used for part of the purchase price, hence avoiding subsequent falls in equity market on this part of the premium
- Spouses' contingent benefits yet to be insured
- Strategic plan - buy-out more pensioners over time, subject to market conditions

# Update at 30 September 2008 - what happened to equity markets?



Index falls by 25%, overseas less in £ terms

# Update at 30 September 2008 - what happened to interest rates and inflationary expectations?



Interest rates and inflation expectations increased

# 2008 valuation - key assumptions

- Assumptions agreed after consultation with the Growth Plan Employer Consultative Group
- Inflation – long term inflation of 3.2%, LPI pension increases 3.0%
- Assumed investment strategy for pensioners
  - 60/40 split of corporate bond/gilt investment
  - Assumed a return of 1% in excess of gilts, i.e. 5.6% per annum
- Assumed investment strategy for non-pensioners
  - Equity investment until retirement, then gilts/bonds
  - Equity returns:
    - ‘Best estimate’ for long term performance - 8.4% per annum
    - Margin for ‘prudence’ - assume 7.6% p.a.
  - Bonds - Gilts plus 0.5% per annum = 5.1% p.a.

# 2008 valuation - valuing liabilities - key assumptions

- Mortality reserves increased to reflect increased life expectancy
  - Results of major occupational study released in 2008 (SAPS)
  - Results compared with a Growth Plan specific mortality study – death rates lower than standard table would indicate
  - SAPS tables adopted for valuation, but adjusted to allow for lower number of deaths
  - Greater allowance for mortality improvements in the future
    - Year of Birth, Long Cohort, 1% underpin
  - Outcome – increase in life expectancy (including future improvements)
    - Male and females reaching 65: +3 years compared to 2005
- Allowance for cash commutation:
  - 50% of members commute 25% of pension on current commutation rates

# Expense reserve

- Need a reserve for future expenses in respect of the Plan
- Fundamentally re-examined
- Pensions Trust anticipate net expenses of £1.3m per annum for 15 years
- Resulting capitalised reserve = 13.3m

# Valuation results – past service position

<b>Assets</b>	<b>£M</b>
<b>Invested Assets (after Paternoster premium)</b>	<b>472.0</b>
<b>Annuity Policies</b>	<b>270.0</b>
<b>TOTAL ASSETS</b>	<b>742.0</b>
<b>Liabilities</b>	
<b>Series 1 - non pensioners</b>	<b>125.5</b>
<b>Series 2 - non pensioners</b>	<b>106.1</b>
<b>Series 3 - non pensioners</b>	<b>246.2</b>
<b>Other deferred pensioners</b>	<b>3.0</b>
<b>Pensioners</b>	<b>270.0</b>
<b>Reserve for pensioner spouses' benefits</b>	<b>6.5</b>
<b>Capitalised value of future expenses</b>	<b>13.3</b>
<b>TOTAL LIABILITIES</b>	<b>770.6</b>
<b>DEFICIT</b>	<b>£28.6m</b>
<b>FUNDING LEVEL</b>	<b>96.3%</b>

# The change in funding position 2005 to 2008

<b>Past service deficit at 30 September 2005</b>	<b>-29.3</b>
Interest on starting deficit for 3 years	-5.4
Return on the market value of the assets compared to assumed return	-41.8
Pensioner buyout	11.5
Data changes	-12.6
Pension increases greater than expected	-2.4
Cash commutation	3.6
Transfer Outs	4.1
Special Contributions	2
Miscellaneous	0.9
<b>Surplus/(Deficit) on 2005 assumptions at 30 September 2008</b>	<b>-69.4</b>
Change in assumptions	40.8
- Expense reserve = 31.6m	
- Financial = 31.5m	
- Mortality = -22.3m	
<b>Surplus/(Deficit) on 2008 assumptions at 30 September 2008</b>	<b>-28.6</b>

# Clearing the deficit of £28.6m at 30 September 2008

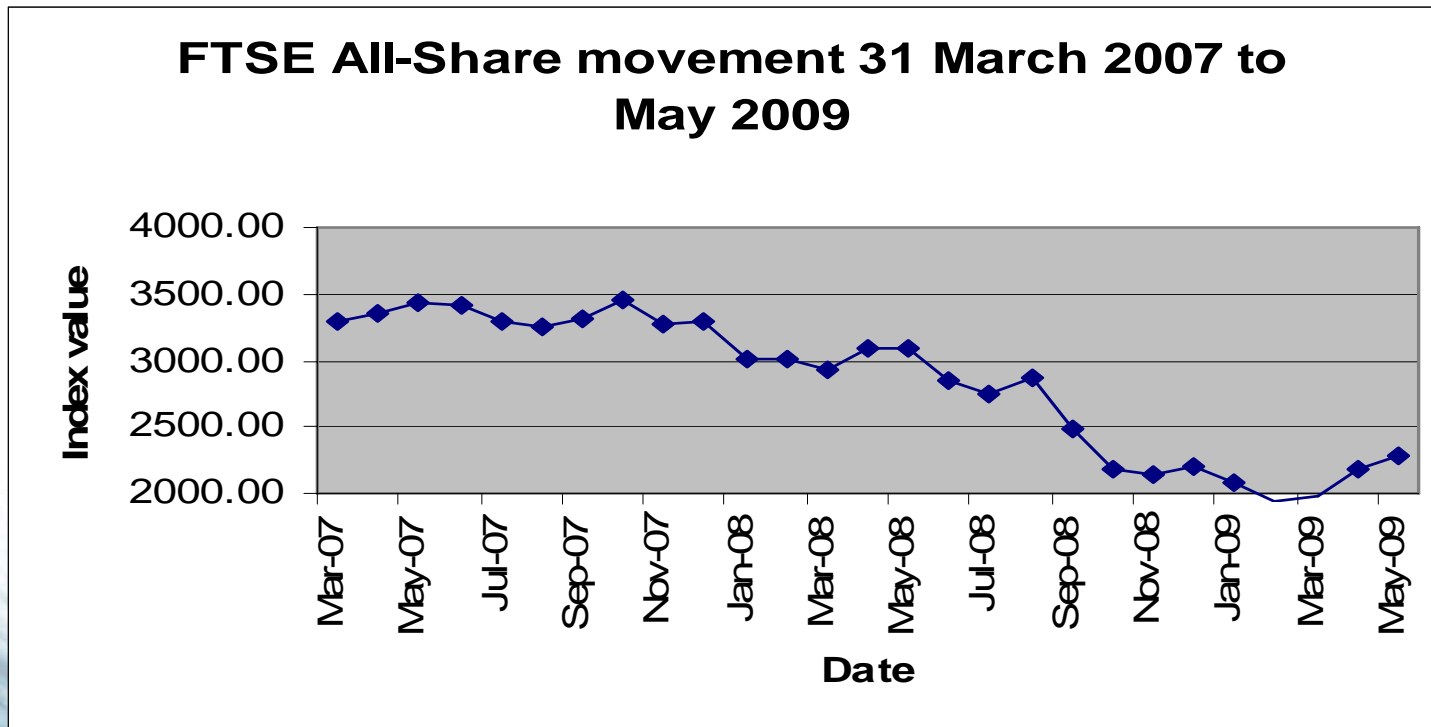
- The deficit would be cleared over 9 years 10 months, if assets perform in line with best estimate assumptions
- Accordingly , the Trustee has decided to not claim employer contributions toward the deficit at this time
- Valuation now needs to be submitted to The Pensions Regulator for clearance

# Buy-out valuation

- Estimate of premium required to transfer remaining liabilities to an insurer if scheme wound-up
- Prospect of immediate wind-up is remote, but buy-out deficit drives Section 75 debt – so very important for some employers
- 30 September 2008, only 2 weeks after Lehman's collapse
- Significant insurer concerns on:
  - Existing corporate bond portfolios
  - Reserve capital required
  - Where to invest going forward
- As a result insurers became much more cautious on pricing for new business
- Extent of increased caution only became apparent gradually, transactions fell significantly
- Required premiums increased
- At the same time scheme investments were falling
- Estimated buy-out deficit at valuation £189m, funding level 79%.
  - Compared with £225m at September 2005 and £118m at March 2007

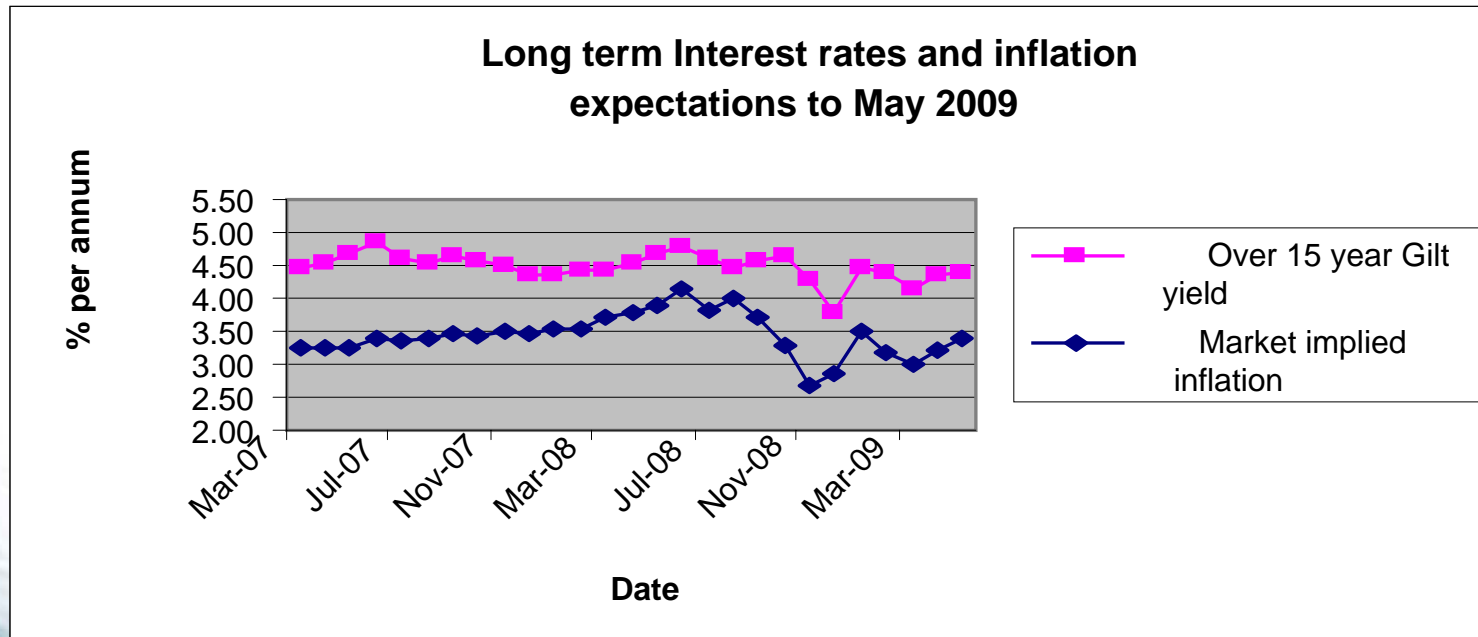
# Financial markets since 30 September 2008

Extreme volatility in equity markets



# Financial markets since 30 September 2008

Extreme volatility in interest rates and inflation expectations



Funding level will have fallen since September 2008

# Summary of Key Issues Going Forward

- Market movements since valuation mean deficits will have increased
- More likely contributions will be needed at the next valuation
- It will depend on market conditions at the next valuation date – 30 September 2011
- Particularly long term interest and inflation rates and equity markets
- Investment strategy reviewed regularly
- Mortality - review new research comprehensively every 3 years
- Opportunity to reduce PPF premium – being investigated now