9 April 2020

Subject: **CRISIS 2020 – UPDATE 4**

Impact on pension funds of current financial markets turmoil and challenges to Europe and global economy

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1. PensionsEurope's statement on the COVID-19 crisis 2020

On Thursday April 9th, PensionsEurope released a statement on the challenges posed by the COVID-19 crisis to pension funds. The statement has been shared with EIOPA and the European Commission.

EU and national actions are crucial in this crisis

The COVID-19 pandemic has resulted in an unprecedented turmoil, which reverberates in the global and European financial markets, and will be followed by recession, high numbers of bankruptcies and rapidly rising unemployment This crisis is symmetric and poses huge challenges for the EU and the Member States. Funded pensions depend on the economy and financial markets and the short-term impact of the crisis is severe. Pension funds are long-term investors with long-term liabilities and with the right policy measures they will be able to get out and recover from this crisis and contribute to financial market stability and the swift recovery of the financial markets and the real economy. It is therefore vital that the EU and Member States do their utmost to alleviate the adverse short-term effects of the crisis.

Many EU countries mainly rely on PAYG social security pensions. Low economic growth and even contraction of the economy will also impact them especially if high unemployment resulting from the crisis turns into lower employment levels. The EU policy to have adequate and sustainable pensions in the future has been based on compensating and complementing lower social security pensions with funded workplace pensions or personal pensions and this will be even more important after the crisis.

Against this background and considering the exogenous nature of the on-going crisis, PensionsEurope and its member associations ask EU level and national regulators and supervisors for close collaboration and support to ensure that pension funds can overcome the challenges posed by the current situation in the financial markets and the severe consequences of the threatening imminent economic downturn. Workplace and personal pensions need to preserve their operational capacities as well as their role to complement public social security pensions and provide adequate and sustainable retirement income.

Measures to alleviate the pressures of funding obligations

The crisis is still in the early days and it is impossible to know how long it will last, which will also differ from country to country. There should therefore be some form of delay on actions that would normally need to be taken (e.g. requirement to produce recovery plan/reduce benefits) until there is a clearer picture of the scale of the crisis and its impact.

The cash flow issues impact on defined benefit (DB) plans as much as on DC plans and possibly more so as in DC plans the contributions required are based on salaries which are being reduced or not paid. The current situation in the financial markets will create new funding pressures and may have impacts on the funding position of pension funds - in particular DB funds, as the value of assets decreases drastically and lower interest rates increase the value of liabilities further. For most DB funds, safety buffers have significantly declined or disappeared, which brings them closer to a possible trigger of recovery plans if the financial markets do not recover in the forthcoming months. It is also vital that pension funds are able to maintain investments that have potential for higher returns, while having the freedom to rebalance their portfolios prudently, taking into account market conditions. Pension funds tend to have a counter-cyclical investment behaviour rather than a pro-cyclical one, therefore contributing to more stable prices in the market during substantial volatility.

EU and national policies should not foster pro-cyclical behavior by IORPs and other pension funds through regulatory requirements as it could destabilize the financial markets, worsen the situation of the real economy. This would very likely force the funds to sell at a loss, which would not be in the interest of the beneficiaries or the sponsors. Depending on the system, this could lead to claims on the sponsoring companies to make additional contributions. The declined liquidity of the sponsor might become a problem.

PensionsEurope welcomes the adoption of specific measures that would provide a certain relief from the pressures arising from funding obligations when they are generated or exacerbated by crisis. The following measures should be considered by National Competent Authorities (NCAs)

- Measures that would ensure that recovery periods are extended in order to allow pension funds to recover their funding position.
- Measures that would provide additional flexibility to pension funds between the moment of observation of the underfunding position and the trigger of recovery actions.
- Measures that would relax the minimum funding or solvency requirements for a certain and limited period of time.

DC schemes do not present solvency concerns even if returns have declined as a result of the shock in the financial markets. Notwithstanding this, the impacts on returns and pension benefits may lead to an increase of withdrawals from voluntary pension plans in those countries where national legislation allows this under specific conditions. DC schemes therefore have to deal with member communications and decumulation options, next to their investments. Many businesses are facing worsening cash flow conditions, which raises specific concerns for pension schemes.

Measures to provide operational relief

Under the current challenging conditions, pension funds need to deal with the effects of the crisis and concentrate their efforts on ensuring business continuity while protecting the health of their own personnel. Business continuity does not necessarily mean business as normal. There may be reduced availability of staff and many may also be carrying out schooling or caring duties at home. There may also be a higher level of enquiries from beneficiaries worried about their pension savings.

PensionsEurope recommends EU authorities and NCAs provide operational relief and postpone non-critical work, where appropriate, in order to alleviate the administrative burden on pension funds during the current crisis.

Flexibility must be provided by NCAs to pension funds as regard the reporting of 2019 year-end and quarterly 2020 data. PensionsEurope recommends EIOPA and the ECB to promote the adoption of such measures by NCAs as EIOPA has done in relation to insurers.

In several Member States, NCAs already adopted specific measures to postpone some supervisory reporting requirements.

- In the Netherlands, the Dutch National Bank indicated it will temporarily relax the supervisory burden on pension funds and already announced that an additional 3 months for reporting of all annual statements will be provided to IORPs.
- In Germany, flexibility is provided for some reporting requirements: the deadline for the submission of the security asset registers (initially March 31st) was suspended. The legally required submission in paper form must be made by June 30th.
- In Bulgaria, the deadline for FSC reporting has been postponed. Some discussions are also underway to explore the possibility to delay some administrative obligations and tax payments.
- Flexibility should also be considered in the organisation of the administrative meetings of pension funds.

We also ask that EU institutions reconsider the deadlines for on-going consultations. The European Commission has already extended the deadlines to respond to relevant on-going consultations. Indeed, the deadline for the consultation on the NFRD review has been postponed to 11 June and the deadline for the consultation on the MiFID II review to 18 May 2020. PensionsEurope welcomes this initiative and recommends a further postponement of these deadlines in case the crisis does not pass. We also urge the EU institutions and NCAs to reconsider the implementation timelines of recently adopted EU legislation, such as the relatively short period for the Disclosure Regulation, either through a delay of the deadline or an accommodating supervisory approach.

PensionsEurope welcomes the extension of deadline agreed by IOSCO and the BCBS for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives, by one year. This extension will provide additional operational capacity for firms to respond to the immediate impact of Covid-19 and at the same time, facilitate covered entities to act diligently to comply with the requirements by the revised deadline.

Measures to support sponsoring companies

Sponsoring companies are under stress as they face a severe shock both on the demand and the supply sides and lack liquidity, which might affect their capacities to fulfil their payment obligations including pension contributions.

PensionsEurope welcomes the adoption of measures that would provide flexibility on the payment of contributions as well as recovery contributions. In some Member States, NCAs already adopted specific measures to alleviate the pressures on sponsoring employers.

- In the Netherlands, the government has decided to provide employers with a compensation, which partly covers the payment of salaries and pension contributions and pension funds will delay the collection of premiums within legally set limits. Similar measures have been adopted in Bulgaria.
- In Germany, it has been decided to postpone to 2021 the payment of recovery contributions by sponsoring employers to Pensionsfonds (one form of IORPs) which are due when the shortfall exceeds 10%.

- In Switzerland, the government has introduced a new ordinance temporarily allowing companies to use an employer contribution reserve for employee contributions as well as employer.

Furthermore, PensionsEurope recognizes the efforts of European authorities to find tools to offset the economic fallout of the pandemic and support companies that are in distress, and welcomes the wide range of fiscal and economic measures that have been adopted at the European level. Since the beginning of the crisis, new measures have been designed to support companies and provide them with additional liquidity with the purpose to save them from bankruptcy. This is vital from a wider economic perspective as well as for the specific case of pension funds considering that sponsoring companies are granted additional support.

PensionsEurope also supports the ambitious fiscal packages and initiatives, which most European Member States have adopted and welcomes the positive stabilising impacts these measures will have on sponsoring companies. These measures include the postponement of social security and tax payments, different kinds of guarantees for new bank loans and additional subsidies, introduction of moratoria of debt repayment due to banks, direct grants to small businesses and public loan guarantees and/or compensation of part of the labour costs for companies (including pension contributions) expecting a certain reduction in their revenues.

2. Impacts on IORPs and measures adopted in MS – (based on various external sources)

The Netherlands

Dutch pensions supervisor De Nederlandsche Bank (DNB) won't object to pension funds deviating from their strategic investment plans during the current extraordinary market conditions. However, recovering pension funds will not be allowed to deliberately and structurally raise the risk profile of their investments. Pension funds should assess whether their current strategic investment policy still matches the risk attitude of their participants. Focus will be increased on crisis management, including continuity management and cyber risks and increased supervision will also target the impact of market volatility on coverage ratios, the implementation of rebalancing policy and liquidity management. Submission of monthly and quarterly reports has already been postponed and on-site investigations are cancelled.

The present assessment is that significant reductions of pension rights and benefits in the Netherlands next year are unlikely, even if coverage ratios don't improve (several pension experts and economists).

In March, coverage ratios of Dutch schemes had dropped to 90% on average. Based on current funding levels, pension benefits could decrease by 15-20%, either as a single discount or spread out over several years. The measure would, for example, hit ABP and PFZW. Recently, Klaas Knot, president of DNB, said it is still too early to discuss rights cuts, as schemes' funding level at year-end is the legal criterion. The negotiators would still be aiming at delivering a framework for a new pensions system before the summer. However, the large funding shortfall in many pension funds is likely to complicate the transition to a new system.

Switzerland

Publica, Switzerland's largest pension fund, is working on three timeframes depicting different scenarios to navigate the COVID-19 crisis (Stefan Beiner, head of asset management). The main question relates to the uncertainties on how long the recession will last: will it be short two to three quarters (V shaped recovery); will it be medium four or six quarters (U shaped recovery); or will it be a long recession six plus quarters (L recession), meaning that sectors and supply chains look completely different compared to today. Publica does not tend to adjust its strategic asset allocation in the event of a U correction, but regularly undertakes a review of the risk-return-assumptions per asset class.

United Kingdom

The Pensions Regulator (TPR) extends deadline for feedback on the first leg of a consultation on the proposed defined benefit funding code; new deadline is 2 September. TPR also updates guidance in relation to the impact of COVID-19 on scheme administration, which is under huge pressures. Points mentioned include the need for vigilance and making sure members are not rushed into any financial decisions.

UK government also announces extension of closing date on consultation on draft non-statutory guidance for occupational pensions on assessing, managing and reporting climate-related risks. New deadline for submissions is 2 July.

TPR and the Financial Conduct Authority, supported by The Money and Pensions Service, jointly warn savers not to rush to make decisions about their pensions in response to the COVID-19 pandemic, and to beware of scams.

UK government extends to 16 July the deadline for responses to a consultation on proposals to expand the dormant assets scheme to include new financial assets, including from pensions.

UK's Pensions Administration Standards Association (PASA) announces new guidance to support administrators during the crisis. Administrators told to concentrate on continuing to pay promised benefits.

Discussions are underway between Reach (largest commercial national and regional news publisher in the UK) and its pension fund's trustees to defer deficit repair contributions following UK Pensions Regulator's recommendation that trustees of DB pension funds should be open to requests to reduce or suspend deficit recovery contributions for no more than three months (or longer depending on the situation).

Denmark

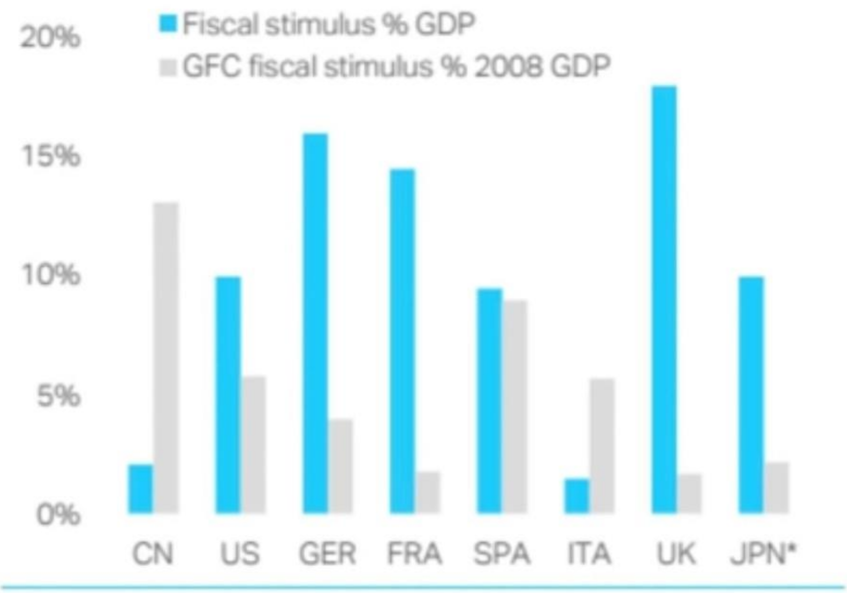
Major pension funds in Denmark are taking a flexible approach to dividend decision-making at companies they invest in. Authorities recognized and understand some commercial enterprises should not be distributing dividends under current circumstances.

Danish pension fund MP Pension gave a tentative prediction that its full-year investment return will come in at below 10%, as it reported an investment loss of 10.1% for the first three months of 2020. MP Pension considers however this drop in returns is reasonable in the current circumstances.

Denmark's PenSam will hold fast to its current investment strategy amid volatile markets shocked by the coronavirus pandemic, with the diversification of its portfolio having guarded it against the worst of market falls in the first quarter.

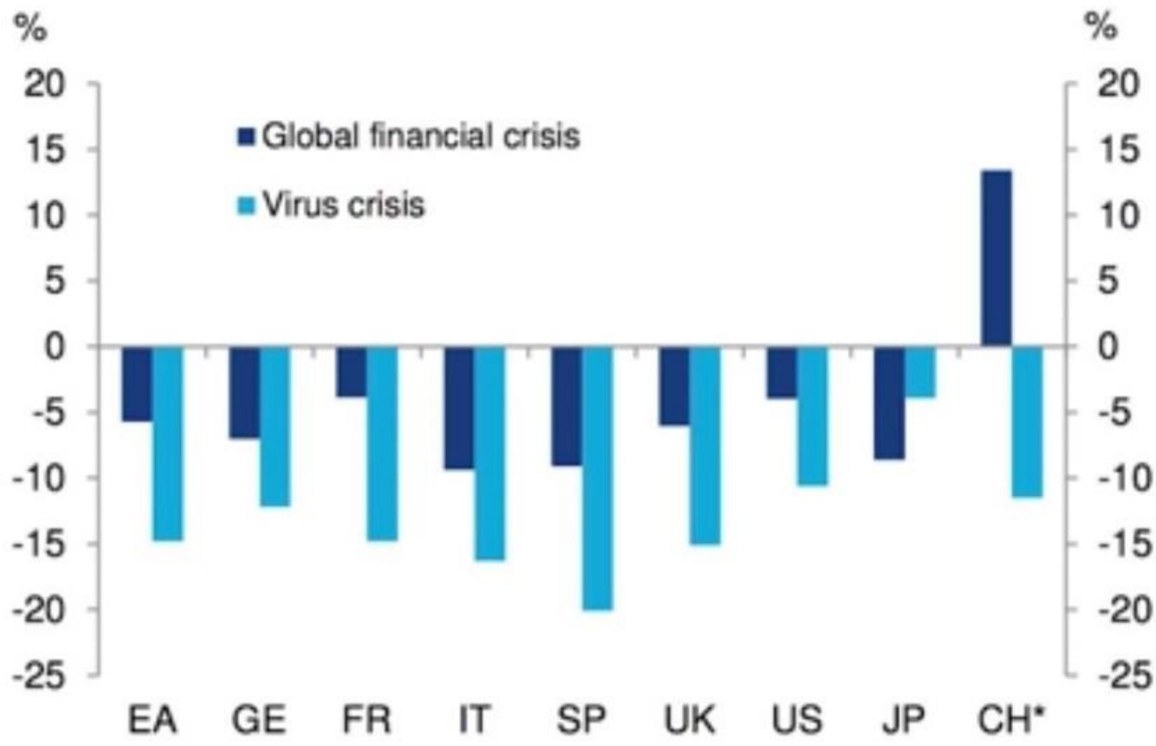
3. Wider economic impact and measures

The recent fiscal stimulus packages of many countries have been enormous. Please find below an interesting Figure comparing (in various countries) fiscal stimulus % GDP (this time) vs GFC fiscal stimulus % 2008 GDP.



Sources: CEIC, OECD, TS Lombard. *Not officially announced.

Also, the (expected) losses caused by the crisis have been huge in many countries. Please find below an interesting economic forecast/statistics by Deutsche Bank on the losses caused by the crisis (% loss from peak to trough) in various countries vs global financial crisis.



Note: China 'GFC crisis' based on GDP growth over the same period the US contracted; 'virus crisis' is Q1 2020 only. Source :Deutsche Bank Research

<u>ECB:</u>

ECB package of temporary collateral easing measures:

- **On 7 April 2020, the ECB adopted a package of temporary collateral easing measures to facilitate the availability of eligible collateral for Eurosystem counterparties to participate in liquidity providing operations, such as the targeted longer-term refinancing operations (TLTRO-III).**
- **The package is complementary to other measures recently announced by the ECB, including additional longer-term refinancing operations (LTROs) and the Pandemic Emergency Purchase Programme (PEPP) as a response to the coronavirus emergency.** The measures collectively support the provision of bank lending especially by easing the conditions at which credit claims are accepted as collateral. At the same time the Eurosystem is increasing its risk tolerance to support the provision of credit via its refinancing operations, particularly by lowering collateral valuation haircuts for all assets consistently.
- **The emergency collateral package contains three main features:**
    1. **First, the Governing Council decided on a set of collateral measures to facilitate an increase in bank funding against loans to corporates and households.** This will be achieved by expanding the use of credit claims as collateral, in particular through the potential expansion of the additional credit claims (ACCs) frameworks.

2. **Second, the Governing Council further adopted the following temporary measures:**
    - A lowering of the level of the non-uniform minimum size threshold for domestic credit claims to EUR 0 from EUR 25,000 previously to facilitate the mobilisation as collateral of loans from small corporate entities;
    - An increase, from 2.5% to 10%, in the maximum share of unsecured debt instruments issued by any single other banking group in a credit institution's collateral pool. This will enable counterparties to benefit from a larger share of such assets.
    - A waiver of the minimum credit quality requirement for marketable debt instruments issued by the Hellenic Republic for acceptance as collateral in Eurosystem credit operations.
        - **So, Greek sovereign bonds will now be accepted as collateral for access to liquidity, however they will still remain rated as 'junk' for international investors. Yet, the move is expected to significantly enhance liquidity in the country, as it will assist the Greek government with its financial response to the pandemic.**
            - The Greek Prime Minister, Kyriakos Mitsotakis welcomed ECB's decision and expressed his hopes that the country will exit the pandemic crisis stronger.
3. **Third, the Governing Council decided to temporarily increase its risk tolerance level in credit operations through a general reduction of collateral valuation haircuts by a fixed factor of 20%.** This adjustment aims to contribute to the collateral easing measures while maintaining a consistent degree of protection across collateral asset types, albeit at a temporarily lower level.

ECB reporting requirements for pension funds:

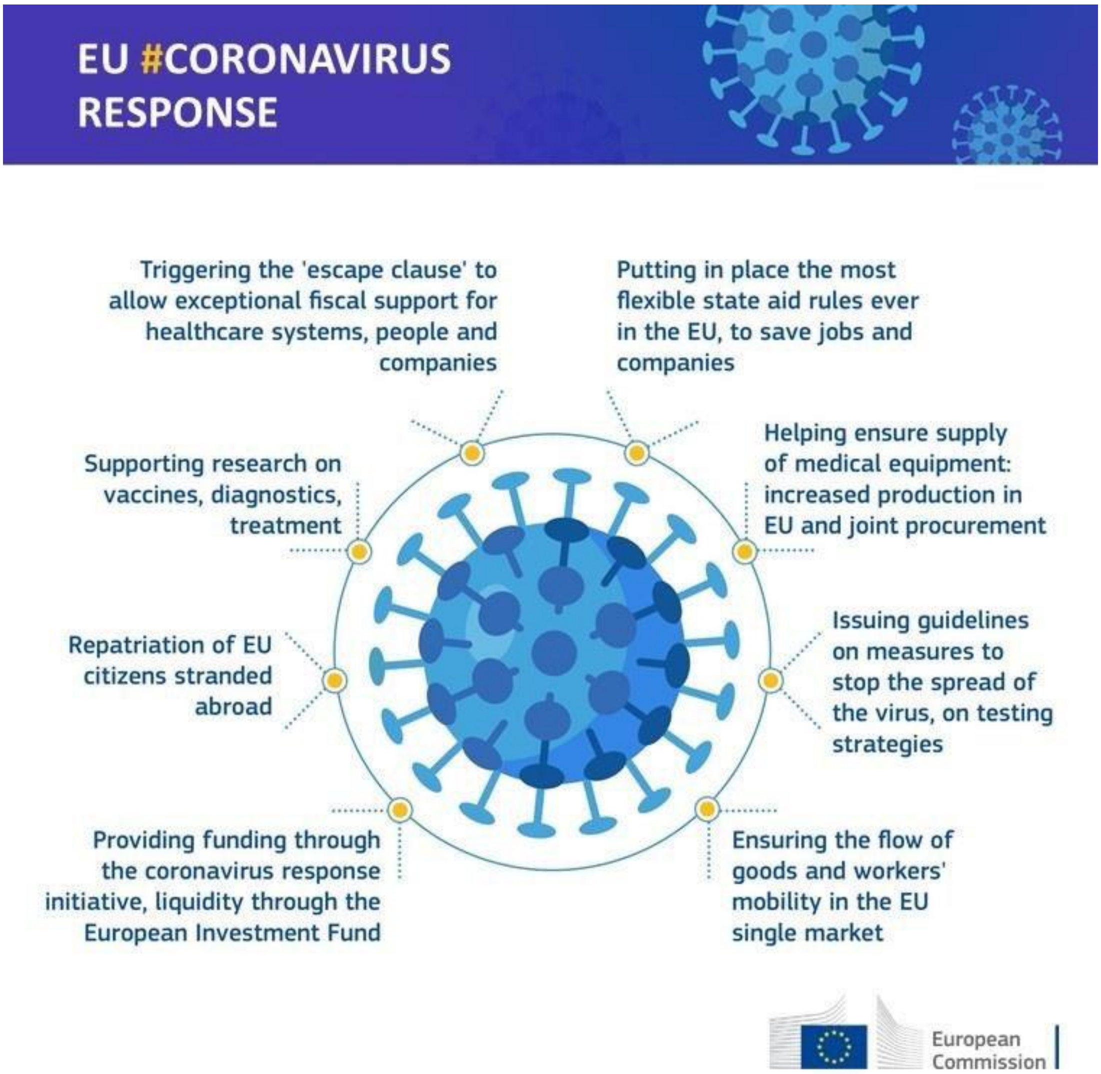
- Recently we have discussed with the ECB about the impact of the crisis on the ECB reporting requirements for pension funds (deadlines, participation etc.) and whether the ECB has considered giving any flexibility to pension funds related to their reporting requirements. Currently the ECB is discussing internally within their WG MFS and also bilaterally with EIOPA, and the ECB aims to inform about their decision in the coming days.

On a side note, oIn several Member States, NCAs already adopted specific measures to postpone some supervisory reporting requirements:

- In the Netherlands, the Dutch National Bank indicated it will temporarily relax the supervisory burden on pension funds and already announced that an additional 3 months for reporting of all annual statements will be provided to IORPs.
- In Germany, flexibility is provided for some reporting requirements: the deadline for the submission of the security asset registers (initially March 31st) was suspended. The legally required submission in paper form must be made by June 30th.

- In Bulgaria, the deadline for FSC reporting has been postponed. Some discussions are also underway to explore the possibility to delay some administrative obligations and tax payments.

EC:



- **To mitigate economic shocks and save businesses, the EC set the most flexible state aid rules yet, allowing EU countries to provide direct support for hard hit companies.**
- **On 8 April 2020, the Commission is launched ESCALAR, a new investment approach, developed together with the European Investment Fund (EIF), that will support venture capital and growth financing for promising companies, enabling them to scale up in Europe and help reinforce Europe's economic and technological sovereignty.**
    - It will provide up to €300 million aiming to increase the investment capacity of venture capital and private equity funds, triggering investments of up to €1.2 billion, or four times the original investment, to support promising companies.

    - With the launch of ESCALAR, the Commission is delivering on one of the actions announced in the new SME strategy to improve access to finance for SMEs. This initiative is particularly relevant in the difficult economic situation SMEs are facing currently due to the coronavirus outbreak. It will support innovative companies during, and after, the crisis, to ensure that Europe can develop and stay at the helm of global technological developments and accelerate its economic recovery.
- **On 8 April 2020, the EC and the High Representative set out plans for a robust and targeted EU response to support partner countries' efforts in tackling the coronavirus pandemic.**
    - The EU's collective action will focus on addressing the immediate health crisis and resulting humanitarian needs, strengthening partner countries' health, water and sanitation systems and their research and preparedness capacities to deal with the pandemic, as well as mitigating the socioeconomic impact.
    - To underpin these actions, the EU will secure financial support to partner countries amounting to more than €15.6 billion from existing external action resources.

EIB:

On 3 April 2020, the Board of Directors of the European Investment Bank (EIB) discussed the creation of a €25 billion guarantee fund to enable the EIB Group to scale up its support for companies in all 27 EU Member States by an additional up to €200 billion. This comes on top of an immediate support package of up to €40 billion announced in March. The Board prepared the proposal for the guarantee fund for discussion by the Eurogroup on the 7th of April 2020 (see more below).

Eurogroup:

- **On 7 April 2020, the EU finance ministers failed to agree on a coordinated EU strategy that would help protect the EU's companies and governments from the economic fallout of the pandemic.** Divisions between factions led by Italy and the Netherlands proved too wide to bridge during the ministers' online Eurogroup meeting, which lasted over 16 hours. The disagreements mainly emerged over conditions for credit lines from the eurozone's bailout fund and the idea of pooling debt through so-called corona bonds.
- **The EU finance ministers will resume on 9 April in a bid to reach a package deal that they can present to prime ministers.**

On a side note on the European Research Council:

Mauro Ferrari, the president of the European Research Council — the EU's top scientist — has resigned after failing to persuade Brussels to set up a large-scale scientific programme to fight Covid-19. Professor Mauro Ferrari, who started a four-year term as leader of Europe's flagship scientific institution on January 1, submitted his resignation to EU commission president Ursula von der Leyen on 7 April. "I have been extremely disappointed by the European response to Covid-19," he said in a statement to the Financial Times. "I arrived at the ERC a fervent supporter of the EU [but] the Covid-19 crisis completely changed my views, though the ideals of international collaboration I continue to support with enthusiasm." The ERC, set up in 2007 to fund Europe's best scientists, has become one of the world's most prestigious funding agencies with a budget of around €2bn a year.

4. Financial markets and European supervisory authorities

a. Banking sector

- **Basel Committee and IOSCO announce deferral of final implementation phases of the margin requirements for noncentrally cleared derivatives**

  IOSCO and the BCBS decided to postpone the deadline for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives, by one year. **PensionsEurope welcomes this initiative since it will provide additional operational capacity for pensions funds** as well as other firms to respond to the immediate impact of Covid-19 and at the same time, facilitate covered entities to act diligently to comply with the requirements by the revised deadline.

- **SSM asks banks not to pay dividends until at least October 2020**

  SSM (ECB banking supervision) updated its recommendation to banks on dividend distributions. To boost banks' capacity to absorb losses and support lending to households, small businesses and corporates during the COVID-19 pandemic, they should not pay dividends for the financial years 2019 and 2020 until at least 1 October 2020. Banks should also refrain from share buy-backs aimed at remunerating shareholders.

b. EIOPA

- **EIOPA extends deadline for stakeholder group applications**

  The European Insurance and Occupational Pensions Authority (EIOPA) is currently seeking applications for its two Stakeholder Groups, the Insurance and Reinsurance Stakeholder Group and the Occupational Pensions Stakeholder Group.
  In light of the challenges and difficulties caused by the Covid-19 pandemic, EIOPA has decided to extend the deadline for interested stakeholders to submit their application.
  The new deadline for applications is now Sunday, 19 April 2020, extended from 13 April.

- **EIOPA statement on dividends distribution and variable remuneration policies in the context of COVID-19**

  EIOPA adds to regulatory pressure on dividend payments, urging insurers to temporarily suspend all discretionary dividend distributions and share buy backs, and to apply a similarly prudent approach to variable remuneration policies[1]. The European Central Bank and Bank of

[1] See Membership Note 08

England had already issued calls for banks to refrain from dividend payments. Earlier this week Morgan Stanley analysts said that based on company announcements so far, companies accounting for 17% of total EU dividends have already cut or suspended payouts.

- **EIOPA publishes extraordinary information for Solvency II Relevant Risk-Free Interest Rate Term Structures and Symmetric Adjustment to Equity Risk with reference to 6 April 2020**

  In the coming weeks, EIOPA will carry out extraordinary calculations on weekly basis to monitor the evolution of the relevant risk-free interest rate term structures (RFR) and the symmetric adjustment to equity risk (EDA). EIOPA is publishing this information in order to support insurance and reinsurance undertakings in the monitoring of their solvency and financial position.

- **EIOPA urges insurers and intermediaries to mitigate the impact of the crisis on consumers, saying unfair treatment of consumers as a result of market disruption was a risk to the entire sector**

  While highlighting the need for flexibility in the interest of consumers and for their continued fair treatment, the EU supervisory authority also noted that imposing retroactive coverage of claims not envisaged within contracts could create material solvency risks and ultimately threaten policyholder protection.

- **Insurance Europe supports GFIA's statement on COVID-19.**

  The Global Federation of Insurance Associations (GFIA) issued a statement on the response of insurers to COVID-19, with the following recommendations for policy actions:

  - Insurers should not be required to cover losses due to pandemics and other causes when coverage was not included in existing policies or reflected in premium payments.
  - When businesses are instructed to close, Governments must act on requests from their national markets for exceptions or other steps that can be taken to allow (re)insurance companies to maintain their operations, so that they can continue to provide the insurance coverage and pension savings products that their customers demand.
  - Coordination between governmental authorities on implementation of additional data requests for information on solvency and business continuity plans – and the allowance of some flexibility to account for existing administrative burdens – will be very important in allowing the industry to concentrate time and resources on serving policyholders and confronting the pandemic.
  - Governments and regulators should relax requirements for paper-based or in-person communication and encourage the digital delivery of insurance documents. The focus should be on customer outcomes, such as the customer receiving the documents, instead of the means by which the customer receives the documents.

c. ESMA

- **ESMA sets out supervisory expectations on publication of investment funds periodic reports**

  While recognising the importance of periodic reports for timely and transparent disclosure, ESMA is of the view that the burdens on Fund Managers associated with the COVID-19 outbreak should be taken into account by NCAs in a coordinated way. In the current situation, ESMA expects NCAs to adopt a risk-based approach and not prioritise supervisory actions against these market participants in respect of the upcoming reporting deadlines.

- **ESMA extends MiFID ii/MiFIR transparency review report consultation to 14 june 2020**

  The decision has been taken in recognition of market participants' current focus on crisis work and their operational constraints, as well as taking into account the technical complexity of the report.