8 May 2020

Subject: **CRISIS 2020 – UPDATE 8**

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

Action required:
For information

1. Impacts on IORPs and measures adopted by NCAs – (based on various external sources)

Earlier this week, PensionsEurope shared with its Members a summary of the measures and actions adopted so far (Membership Note 2020/15).

The Netherlands

Some of the largest Dutch pension funds have reported losses ranging from 5.8% up to 10.2% for the first quarter of the year.

- Progress, the Dutch pension fund for Unilever, has incurred a 10.2% loss on investments in Q1 2020. The funding level for its closed DB scheme has dropped 19 percentage points to 110% and its policy coverage dropped to 124%. Its Dutch DC plan has lost 5.8% in Q1 2020. Its funding level has plummeted by 20 percentage points to 104% and its policy coverage dropped to 120%.
- Multi-sector pension fund PGB posted a quarterly return of -8.3%, and a policy coverage of 100.6%.
- The Philips Pensioenfonds saw its assets decline by 6.6% in Q1 2020, due to losses on its 42.5% securities holdings. Its policy coverage stood at 104.4%.

ABP posted a loss on investments of 9.8% in Q1 2020 and said its participants had to prepare for significantly higher contributions in the coming years, as pensions provision had become too expensive for the current arrangements. The current premium of 24.9% are too low given the low interest rates and the expected lower returns. ABP's board has already decided to gradually reduce the discount rate for the scheme's future expenses from the current 2.8% to 2% as of 2023.

Reported losses at other large industry-wide schemes ranged from 8.8% for the healthcare pension fund PFZW to 5% for BpfBouw, the scheme for the building sector.

Germany

According to VAG (Insurance Supervision Act), German IORPs are required to provide a statement on the principles of their investment policy four months after the end of a financial year at the latest, or immediately after a major change in investment policy. BaFin will not object if IOPRs would not follow the requirement in 2020.

UK

The spring edition of the quarterly pension publication of Aon In Sight provide an excellent summary of the measures adopted by the UK Pension Regulator (TPR) and by the UK government to mitigate the impact of Covid 19 on UK pension funds. You can access the publication at this link.

Finland

Ministry of Social Affairs and Health has prepared a bill on the temporary strengthening of pension insurers' solvency. The precautionary bill included three different measures that could be used to strengthen the solvency capital of occupational pension insurers, which would make it possible for the providers to avoid having to sell their investment assets to a significant extent in an unfavourable market situation. The idea is that the proposal can be submitted to parliament immediately if average solvency plummets.

Solvency capital at the country's two largest pension insurance companies, Ilmarinen and Varma, have fallen by 25% and 30% respectively in Q1 2020, but ratios remained well above minimum requirements for both companies.

Varma suffered a 10 % loss on its investments in Q1 2020 but its solvency ratio remains high.

Norway

Kommunal Landspensjonskasse (KLP), Norway's main provider of municipal pensions, reported a 3.7% investment loss in the first quarter of this year.

Denmark

Two of Denmark's largest commercial pension funds, PFA and Danica Pension, have reported steep investment losses of 10.5% and 15.4% respectively in Q1 2020. ATP posted a -26% investment return in Q1 2020.

Peru

A new law allows participants to withdraw up to 25% of their private retirement assets to help them cope with the impacts of the coronavirus pandemic.

2. Results of PLSA survey

The **Pensions and Lifetime Saving Association (PLSA)**, published the results of a survey conducted among their members between 8 and 18 April 2020. The results suggest that UK pension funds are coping well with the COVID-19 crisis:

- Almost two-thirds (62%) believe COVID-19 is having little impact on the day to day running of the scheme (up from 39% in March).
- Almost all schemes' contingency plans are coping (99%).
- All schemes are confident that they can meet their payment obligations to members over the coming months, with 85% reporting that they are "very confident" and the remainder (15%) that they are "fairly confident".
- There is increasing confidence in the ability of their Third Party Administrator's capacity to service the needs of their members (68% have no concerns compared with 60% in March).
- Fewer are concerned about the strength of their scheme sponsor/employer (45% are not concerned at all, compared with 29% in March).

You can read the full report at this link.

3. UK Pension Policy Institute briefing note

The UK **Pension Policy Institute** has published a briefing note on the pension policy implications of Covid-19. The note explores the impact that the coronavirus may have on pensions now and in the future. It explores likely impacts in terms of:

- Stock market volatility and its effects on DC pot sizes and DB scheme sponsors' ability to deliver on member promises.
- Employment and the Government Job Retention Scheme.
- The effects on different age groups, including younger workers, those approaching retirement and those already in retirement.

Main conclusions:

- For DC scheme members, remaining invested in their scheme's default fund may provide some protection from large reductions in pot size.
- For DB scheme members, TPR's three month delay on transfers offers protection from decisions that could have a negative impact on future retirement incomes, including the increased risk of scams.
- Those approaching or already in retirement could benefit from delaying or reducing withdrawals from their pension pot, if possible, in order to mitigate the impact of current stock market volatility.
- Any potential increases in unemployment and lower pension contributions from employers and employees as a result of the current crisis will reduce future DC pension income, and reduce security for DB scheme members, meaning that the pensions impact could continue for many years to come.

You can read the full briefing note at this link.

4. Economic outlook

- **Eurozone/EU: On 6 May, the EC published its** Spring 2020 Economic Forecast projecting that the euro area economy will contract by a record 7¾% (earlier the IMF forecasted almost the same (7½ %)) in 2020 and grow by 6¼% in 2021. **The EU economy is forecast to contract by 7½% in 2020 and grow by around 6% in 2021** Growth projections for the EU and euro area have been revised down by around nine percentage points compared to the Autumn 2019 Economic Forecast.
- **The UK: The Bank of England has forecast the UK economy will contract by a historic 30 per cent in the first half of year but has decided not to launch new stimulus moves.** In its monetary policy report, the UK's central bank presented an indicative forecast for the economy, predicting that output would dip 3 per cent in the first quarter followed by a further 25 per cent fall in the second, making a 30 per cent drop overall in the first half.

5. Economic measures

- On May 4, the ECON Committee of the European Parliament published **the latest state of play of EU/EA measures to mitigate the economic, financial and social effects of coronavirus**.
- On 5 May, the ECON Committee hold exchanges of views with Elke König , Chairperson of the Single Resolution Board (SRB) and with Andrea Enria, Chair of the Supervisory Board of the ECB, on the economic impact and the response to the COVID-19 pandemic. Both stressed that the European banking system is in a far better position to deal with this crisis than the 2008 financial crisis and detailed how their institutions had reacted to the pandemic. Enria stressed that the focus has to be on ensuring that the banks can continue lending to the real economy to protect against any productivity losses which would hinder any economic recovery.

- **Video conference of the Eurogroup, 8 May 2020:** The Eurogroup will e.g. discuss:

- The economic situation of the euro area based on the above-mentioned EC spring forecast. The discussion will inform the Eurogroup's efforts to tackle the COVID-19 crisis, and prepare the ground for the recovery of the euro area economy, and;
- The main features of the Pandemic Crisis Support instrument of the European Stability Mechanism. The aim is for the instrument to be operational by 1 June, as indicated by the President of the European Council following the videoconference of the members of the European Council on 23 April.

6. Monetary policy

On 30 April, the ECB took the following important monetary policy decisions:

1. **The conditions on the targeted longer-term refinancing operations (TLTRO III) have been further eased.** Specifically, the Governing Council decided to reduce the interest rate on TLTRO III operations during the period from June 2020 to June 2021 to 50 basis points below the average interest rate on the Eurosystem's main refinancing operations prevailing over the same period.
2. **A new series of non-targeted pandemic emergency longer-term refinancing operations (PELTROs) will be conducted to support liquidity conditions in the euro area financial system and contribute to preserving the smooth functioning of money markets by providing an effective liquidity backstop.** The PELTROs consist of seven additional refinancing operations commencing in May 2020 and maturing in a staggered sequence between July and September 2021 in line with the duration of the collateral easing measures.
3. Since the end of March, purchases have been conducted under the Governing Council's new pandemic emergency purchase programme (**PEPP**), which has an overall envelope of €750 billion, to ease the overall monetary policy stance and to counter the severe risks to the monetary policy transmission mechanism and the outlook for the euro area posed by the coronavirus pandemic. **These purchases will continue to be conducted in a flexible manner over time, across asset classes and among jurisdictions. The Governing Council will conduct net asset purchases under the PEPP until it judges that the coronavirus crisis phase is over, but in any case until the end of this year.**
4. **Moreover, net purchases under the asset purchase programme (APP) will continue at a monthly pace of €20 billion, together with the purchases under the additional €120 billion temporary envelope until the end of the year.** The Governing Council continues to expect monthly net asset purchases under the APP to run for as long as necessary to reinforce the accommodative impact of its policy rates, and to end shortly before it starts raising the key ECB interest rates.
5. **Reinvestments of the principal payments from maturing securities purchased under the APP will continue**, in full, for an extended period of time past the date when the Governing Council starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

6. **The interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will remain unchanged at 0.00%, 0.25% and -0.50% respectively. The Governing Council expects the key ECB interest rates to remain at their present or lower levels until it has seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2% within its projection horizon, and such convergence has been consistently reflected in underlying inflation dynamics.**
7. **The Governing Council is fully prepared to increase the size of the PEPP and adjust its composition, by as much as necessary and for as long as needed. In any case, it stands ready to adjust all of its instruments, as appropriate, to ensure that inflation moves towards its aim in a sustained manner, in line with its commitment to symmetry.**

- Furthermore, **on 5 May, the ECB published a** press release **in which it takes note of German Federal Constitutional Court** ruling. The ECB Governing Council stresses that it remains fully committed to doing everything necessary within its mandate to ensure that inflation rises to levels consistent with its medium-term aim and that the monetary policy action taken in pursuit of the objective of maintaining price stability is transmitted to all parts of the economy and to all jurisdictions of the euro area.

7. Recent regulatory developments and actions in the financial markets

OTC derivatives

- **ESAs amend the bilateral margin requirements under EMIR in response to the COVID-19 outbreak**

  The ESAs have published joint draft RTS to amend the Delegated Regulation on the risk mitigation techniques for non-centrally cleared OTC derivatives, under EMIR, to incorporate a one-year deferral of the two implementation phases of the bilateral margining requirements. These changes would result in covered counterparties with an aggregate average notional amount of non-centrally cleared derivatives above €50 bn becoming subject to the requirement to exchange initial margin from 1 September 2021, while covered counterparties with an aggregate average notional amount of non-centrally cleared derivatives above €8 bn becoming subject to the requirement from 1 September 2022.

  This announcement follows a joint decision by IOSCO and BCBS to postpone the deadline for completing the final two implementation phases of the margin requirements for OTC derivatives[1].

  PensionsEurope welcomes this initiative since it will provide additional operational capacity for pensions funds and other firms that fall under the two last implementation phases of the bilateral margin requirements 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.

Banks – Q1 2020 quarterly results

- **ING profit falls 40%, provisions rise**

[1] See membership note 9, crisis update 4

Dutch bank ING reported a first-quarter net profit that fell sharply as the bank's provisions to cover potential soured loans more-than tripled and revenue slipped. ING added 661 million euros to its provisions for bad loans. For the same period last year, the figure was EUR207 million.

- **France: decline in Q1 2020 results**
  BNP Paribas' profit fell by 33.1% in the first-quarter as the coronavirus crisis hit equity trading and prompted the bank to set aside more than half a billion euros in loan provisions.
  Credit Agricole reported today a 16.4% decline in quarterly profit, the amount of provisions to protect itself from potential loan defaults almost tripled.
- **Italian banks report mixed Q1 results**
  UniCredit reported the second loss in a row as provisions related to the coronavirus, job cuts and writing off its Turkish unit. The net loss totaled 2.71 billion euros as loan-loss provisions climbed to 1.26 billion euros. Intesa SanPaolo reported a surprise 10% rise in first-quarter net profit thanks to strong trading gains. Italy's second bank expects to make a net profit of at least 3 billion euros this year after writing down loans for half that figure
  Monte dei Paschi di Siena posted a 244 million euros loss in the first quarter after writing down loans due to the economic fallout from the pandemic. Banco BPM reported a better than expected first-quarter net profit and said it would set new targets to take into account the virus fallout. Handelsblatt states that most Italian banks have the worst still ahead of them and the next balance sheet season will show this much more clearly than before.
- **Spain's banks to take further profit hit**
  Spanish banks' profits are expected to continue falling sharply in the coming months as demand for mortgages and consumer finance slump, and provisions for bad loans rise amid the coronavirus pandemic. Five of Spain's largest lenders posted a sharp drop in profits in the first quarter of the year, according to S&P Global Market Intelligence data. Santander has posted an 82% year-on-year slump in quarterly net profit as it booked a provision of 3.9 billion euro.
- **European banks could be forced to merge earlier than expected** (Javier Oficialdegui, the co-head of UBS's investment banking unit)

Insurers

- **EIOPA revises its timetable for advice on Solvency II Review until end December 2020**
  EIOPA, in close coordination with the European Commission, has decided to deliver its advice to the European Commission at end December 2020, to take into account the importance of assessing the impact of the current Covid-19 situation on the Solvency II Review.

Investor protection

- **ESMA reminds firms of conduct of business obligations under MiFID II**
  ESMA is issuing a Public Statement on the risks for retail investors when trading under the highly uncertain market circumstances due to the COVID-19 pandemic. ESMA also reminds investment firms of the key conduct of business obligations under MiFID when providing services to retail investors.