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Press Release

Survey shows Pension Schemes making considerable progress in De-Risking

Smaller Schemes still favour higher Risk
Risk Reserve requirement putting stress on schemes

A major survey of DB pension schemes, conducted by EY, in conjunction with the Irish Association of Pension Funds (IAPF), on attitudes towards pension scheme risk [1] found that;

- Pension funds still have a lot of assets that are return seeking and therefore more risky, though considerable progress has been made on de-risking the funds.
- Larger schemes tend to be more conservative and have made more progress on de-risking, perhaps because these schemes might be more mature but also perhaps due to the level of time and expertise that can be offered too them.
- The volume and consistency of regulatory change is seen as the biggest single risk to scheme governance
- In seeking to control overall costs 80% opt to close the scheme to new joiners; 26% cap salary increases; 21% restrict future accrual; 1/5 of employees subject to increased contributions.

The survey of DB pension schemes has revealed that the introduction of the Funding Risk Reserve has resulted in schemes facing more stringent funding targets to protect against future market volatility. Findings showed that 75% pension schemes have reviewed (40%) or are currently reviewing (35%) their investment policy in light of the new requirements, while a further 14% have begun these discussions. Of these, 45% had carried out a detailed review of investment policy while 27% had carried out a joint review of the scheme's investment and funding policies.

According to Jerry Moriarty, CEO of the IAPF, "This demonstrates the significant impact that the Funding Risk Reserve is having on pension scheme management. The Risk Reserve is a laudable belt & braces concept but the timing couldn't be much worse. The requirement seems to be having a significant impact on these schemes and could question their long-term viability.

The survey reveals that larger schemes tend to be more conservative and have made more progress on de-risking though there is some concern that pressure to continue to de-risk could ultimately restrict long-term returns which in turn could affect pension benefits."

Iain Brown, Partner with EY commented, "Risk and the management of risk has always been a core part of governing and managing pension schemes. We believe that the Funding Risk Reserve will result in scheme trustees and sponsoring companies taking a more integrated approach to pension scheme funding and investment."

Asset Allocation Strategies

- Larger schemes tend to be more conservative and have made more progress on de-risking.
- Smallest schemes with fund sizes of £10m to £25m generally held a significantly higher proportion of their assets (an average of around 58%) invested in return-seeking assets.

- As schemes mature and the volume of pension payments increase, the allocation to return-seeking assets tends to decrease, due to the need for more predictable, income-producing assets such as bonds.
- The average scheme holds around 47% of assets in return-seeking assets, young schemes typically hold around 50% in return-seeking assets, versus an average of 43% for mature schemes.

Jerry continued, "The survey showed that while asset allocation strategies differ between younger and older schemes it is not to the extent that would be expected with a modest difference in allocations to return-seeking assets being noted".

Jerry went on to say, "The balance between return-seeking and matching assets is a much debated point – too risky could result in significant losses, but too conservative will restrict long-term growth vital to deliver the promised pensions".

According to Iain, "Perhaps one would expect smaller schemes to have more of a focus on return-seeking assets if these schemes are also young , however, part of the reason could simply be that smaller schemes have less resource and expertise to devote to the pension risk agenda. Nevertheless, we would expect the trend towards achieving a more matched, liability driven investment portfolio, which relies less heavily on outperformance from return-seeking assets, to continue over time".

Controlling future pension costs

Most of the pension schemes surveyed had taken measures to control future costs, with 80% opting to close the scheme to new joiners. 26% had capped salary increases for active members, 21% restricting future accrual with 21% increasing employee contributions. The full closure of schemes to future accrual is also gathering pace, with around 21% of schemes indicating this as a planned future action.
Other schemes have also been taking action to control costs by reducing members' past service benefits.
Iain added, "The next wave of change is likely to come in the form of full closure to future accrual, or a reduction in the level of future service benefits offered. Schemes with a large number of current employees may look to capping salaries as a way of controlling cost and reducing risk."

Biggest risks to good governance

The volume of regulatory change was identified as the three biggest risks to good governance, with 69% of respondents listing this as a top three factor. Also featuring highly in the responses were lack of trustee expertise, listed by 67% of respondents, and lack of trustee time, listed by around 50% of respondents.

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Notes to the Editor

About IAPF

Established in 1973, the Irish Association of Pension Funds (IAPF) is a non- profit, non-commercial organisation whose aim is shape pensions that are secure, fair and simple.

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[1] *Over 50 schemes of all sizes were involved with assets under management ranging from €10 million to over €1 billion. Around 50% of the schemes surveyed currently meet the Minimum Funding Standard (MFS).*