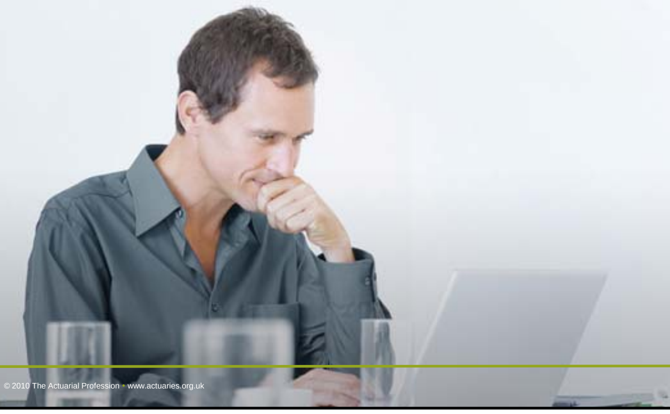
The Actuarial Profession
making financial sense of the future

PPF – an update
Stephen Rice and Andrea Mendham



1 November 2012

© 2010 The Actuarial Profession • www.actuaries.org.uk

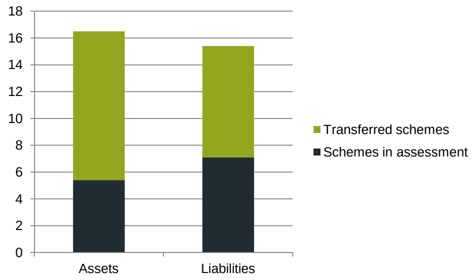
Agenda

- Annual Report and Accounts highlights
- Progress of funding level since 31 March 2012
- Funding strategy recap
- Progress towards 2030 self-sufficiency
- 2012/13 and 2013/14 levy
- Questions

© 2010 The Actuarial Profession • www.actuaries.org.uk

31 March 2012 Annual Report and Accounts - headlines

- Funding level – 106.9%
- Liabilities - £15.4 billion
- Assets - £16.5 billion



© 2010 The Actuarial Profession • www.actuaries.org.uk

Experience items – 31 March 2011 to 31 March 2012

- Surplus at start of year: £680m
- Investment return: +£2,400m
- Changes to assumptions: -£1,800m
- Interest on the liabilities: -£400m
- Levy income: +£600m
- New claims: -£300m
- Other items: -£100m
- Surplus at end of year: £1,070m

© 2010 The Actuarial Profession • www.actuaries.org.uk

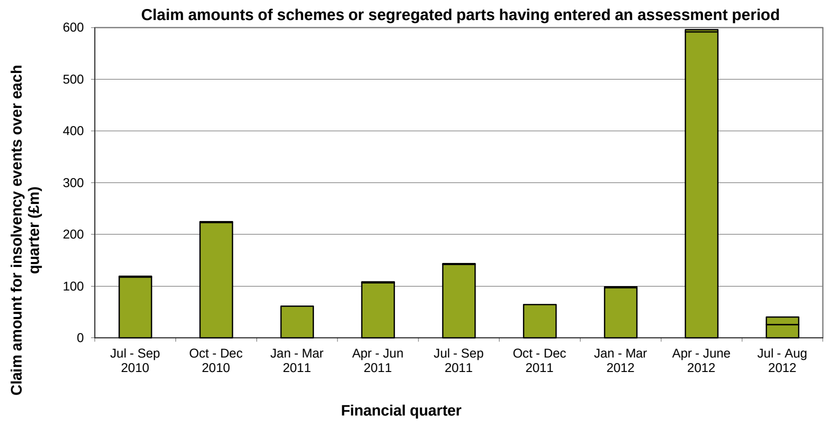
Progress since March 2012

- Funding level at 31 March 2012 – 107%
- Funding level at 31 August 2012 – 103%
- A number of large claims on the fund
- Contingent Liabilities of £1.1 bn at 31 March 2012 as disclosed in the ARA
  - in respect of schemes where we were expecting a claim

© 2010 The Actuarial Profession • www.actuaries.org.uk

4

Claims amounts have risen sharply in recent months



© 2010 The Actuarial Profession • www.actuaries.org.uk

5

The PPFs funding strategy

- Quantitative framework to capture key risks
- First published August 2010
- First update published November 2011
- Most recent update published October 2012
- Update to stakeholders on progress to our vision
- Our vision is to protect people's future
- We need enough money to pay members
- End of August: 103% funded
- What about the future?

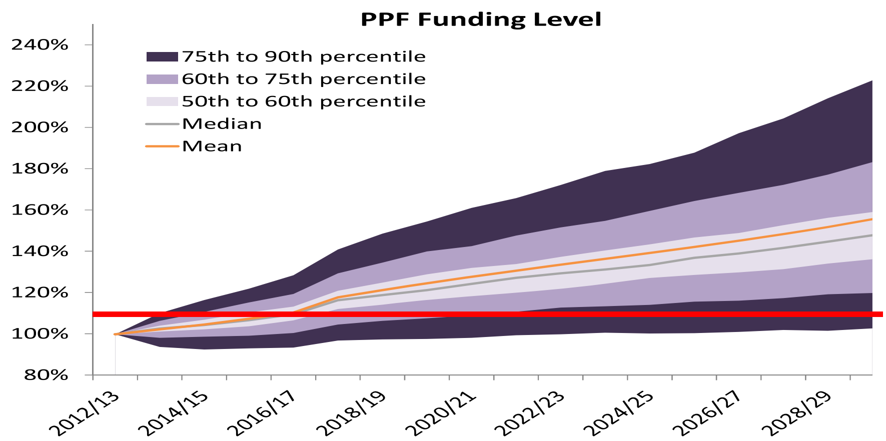
© 2010 The Actuarial Profession • www.actuaries.org.uk

The PPFs funding objective

- Our funding objective is to be financially self-sufficient by 2030.
- This means being 110% funded in 2030
- By 2030, future claims would be low relative to the size of the PPF; PPF levy will be less significant
- The 10% margin covers residual risks
- Our key metrics
  - probability of success = probability of being at least 110% funded in 2030 (84% in March 2012)
  - downside risk: the 90% percentile of projected PPF deficits over the period to 2030 (£10bn in March 2012)

© 2010 The Actuarial Profession • www.actuaries.org.uk

The PPFs funding objective



© 2010 The Actuarial Profession • www.actuaries.org.uk

8

Developments since the previous update in November 2011

- Economic turmoil – larger deficits from schemes
- IORP Directive (‘Solvency II for pension schemes’)
- Central clearance of OTC derivatives
- PPF levy: set at £630m, below £685m limit
- Potential changes to RPI formula
- 84% in March 2012, fall from 87% last year

© 2010 The Actuarial Profession • www.actuaries.org.uk

9

Stress tests

- Downside scenario: Euro shock recession
  - UK recession in the short term, later recovery
  - asset returns and bond yields fall
  - higher insolvency probabilities
  - short-term spike in claims on the PPF
- Upside scenario: export-led recovery
  - strong growth in UK exports to emerging economies
  - higher investment and household spending, drop in oil prices
  - lower unemployment, inflation under control

© 2010 The Actuarial Profession • www.actuaries.org.uk

Stress tests

Scenario	Probability of success	Downside risk
Base case	84%	£10bn
Euro shock recession	76%	£21bn
Export-led recovery	93%	£3bn

© 2010 The Actuarial Profession • www.actuaries.org.uk

A reminder on the New Levy Formula

- Feedback from consultation:
  - More predictability in individual bills
  - Stability of levy bills also a priority
  - Levy should focus more on things schemes can actually control:
    - Funding position
    - Potentially investment strategy
    - i.e. Levy reflects their own risk, not others
  - More transparency on cross-subsidy
  - Stronger link to commercial charging – market consistency

© 2010 The Actuarial Profession • www.actuaries.org.uk

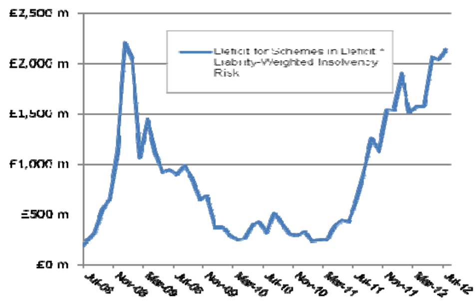
A reminder on the new levy formula

- Bottom up approach
  - total levy is sum of individual levies
  - more predictable levy bills
  - rules and factors adjusted in limited circumstances only.

- New approach to risk measurement
  - smoothing of scheme funding and insolvency risk
  - market-consistent rates for insolvency
  - takes account of investment risk.

© 2010 The Actuarial Profession • www.actuaries.org.uk

PPF risk has risen sharply



© 2010 The Actuarial Profession • www.actuaries.org.uk

Contingent Assets experience in 2012/13

- Levy estimate assumptions for Contingent Assets:
  - re-certifications reduce levy quantum by c.£220m
  - New Contingent Assets reduce levy quantum by c.£40m
- Experience in 2012/13 differs significantly from assumptions:
  - value of re-certifications down 15% or c.£30m
  - value of new guarantees down 50% or c.£20m

Type	11/12	Re-certified	New for 2012/13	Total 12/13
A	785	589 (61 modified)	157	746
B	117	99	30	129
C	17	6	2	8

© 2010 The Actuarial Profession • www.actuaries.org.uk

Levy case studies

Scheme	11/12 levy	12/13 levy	Change %	Comments
Scheme A	100	1,231	1,131	Contingent Asset withdrawn for 12/13 and poorly funded
Scheme B	100	328	228	High risk investment strategy and poorly funded. Strong covenant.
Scheme C	100	201	101	Quite low risk investment strategy, pays RBL for first time.
Scheme D	100	55	-45	Low risk investment strategy and very well funded.
Scheme E	100	30	-70	De-risked investment and well funded.

© 2010 The Actuarial Profession • www.actuaries.org.uk

16

The Actuarial Profession
making financial sense of the future

© 2010 The Actuarial Profession • www.actuaries.org.uk

In summary

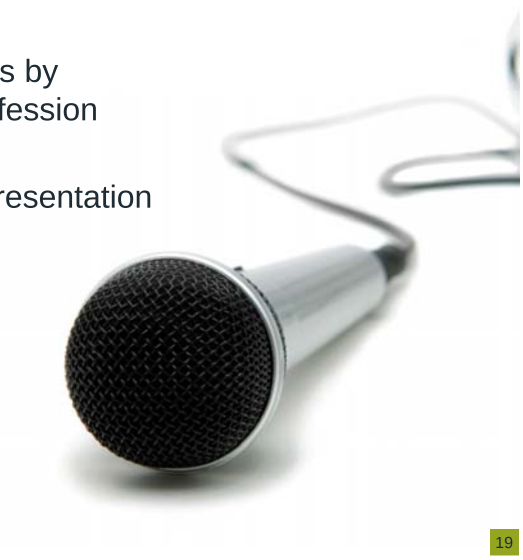
- Scheme funding has deteriorated significantly
- If our protection regime is to remain credible, then it needs to be properly funded
- YTD claims already exceed levy
- Contingent assets remain a concern
- Levy held this year, but next year a 10% increase is likely without a change in markets

© 2010 The Actuarial Profession • www.actuaries.org.uk

Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenter.



© 2010 The Actuarial Profession • www.actuaries.org.uk