The Actuarial Profession

making financial sense of the future

PPF – an update
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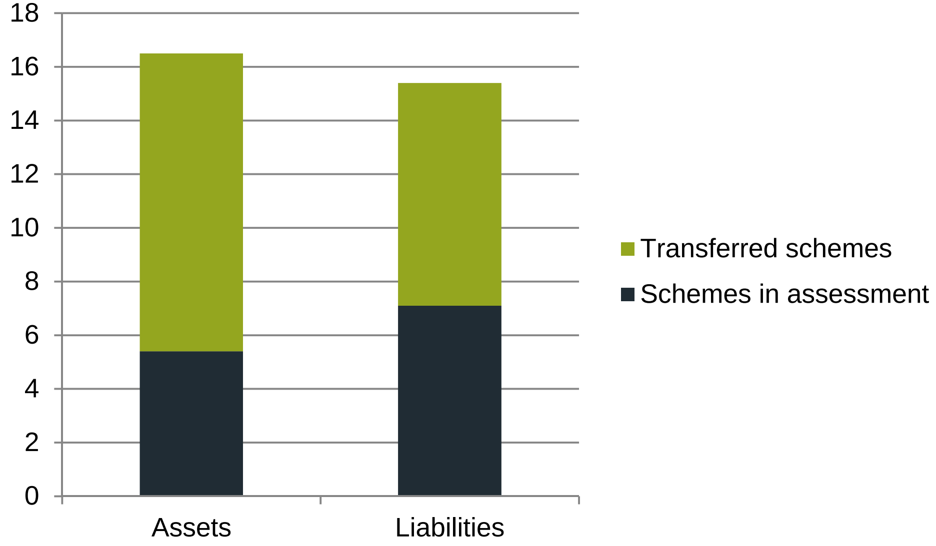
26 November 2012

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

31 March 2012 Annual Report and Accounts - headlines

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



Experience items – 31 March 2011 to 31 March 2012

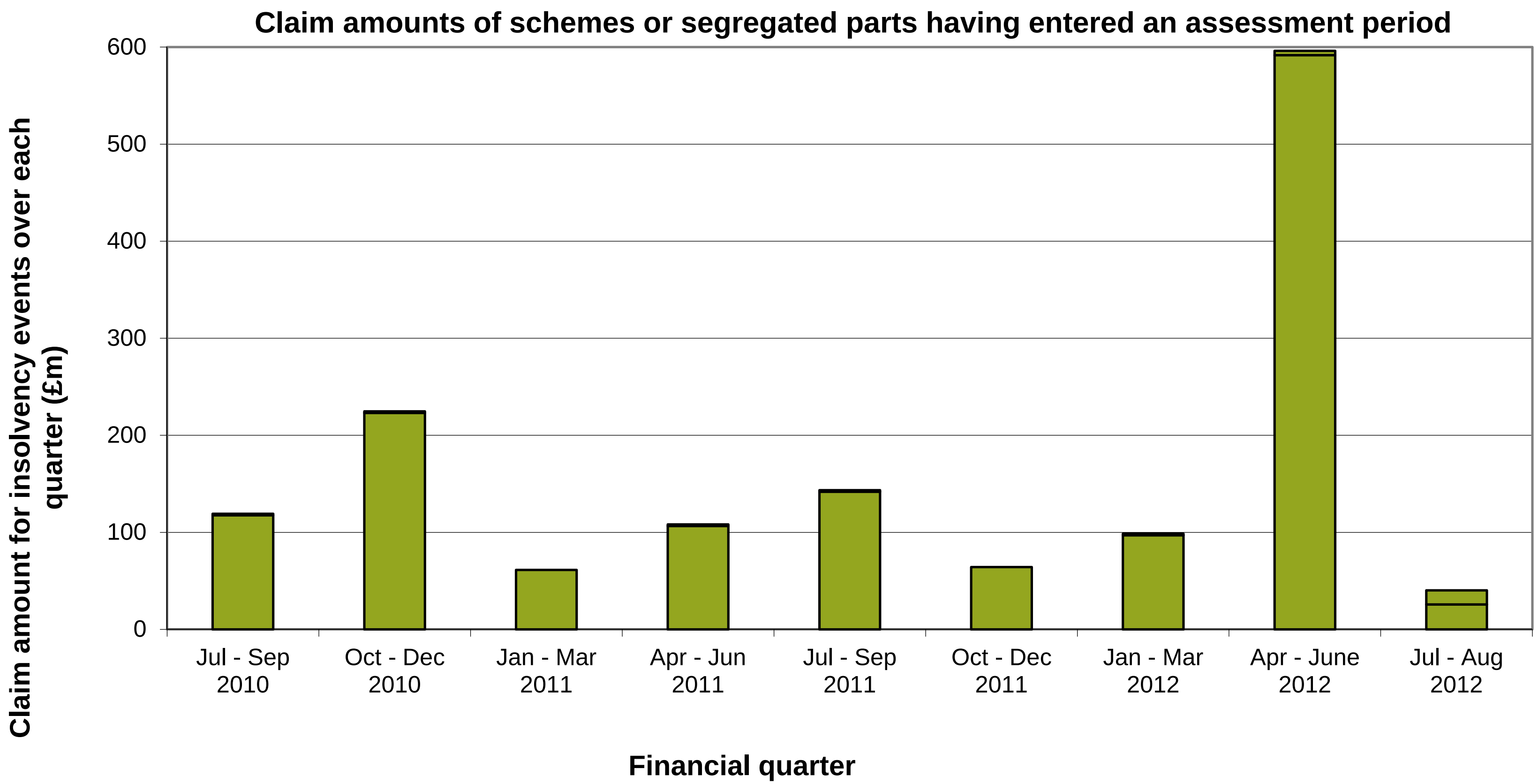
- Surplus at start of year: £680m
- Investment return: +£2,400m
- Changes to assumptions: -£1,800m
- Interest on the liabilities: -£400m
- Levy income: +£600m
- New claims: -£300m
- Other items: -£100m
- Surplus at end of year: £1,070m

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

Claims amounts have risen sharply in recent months



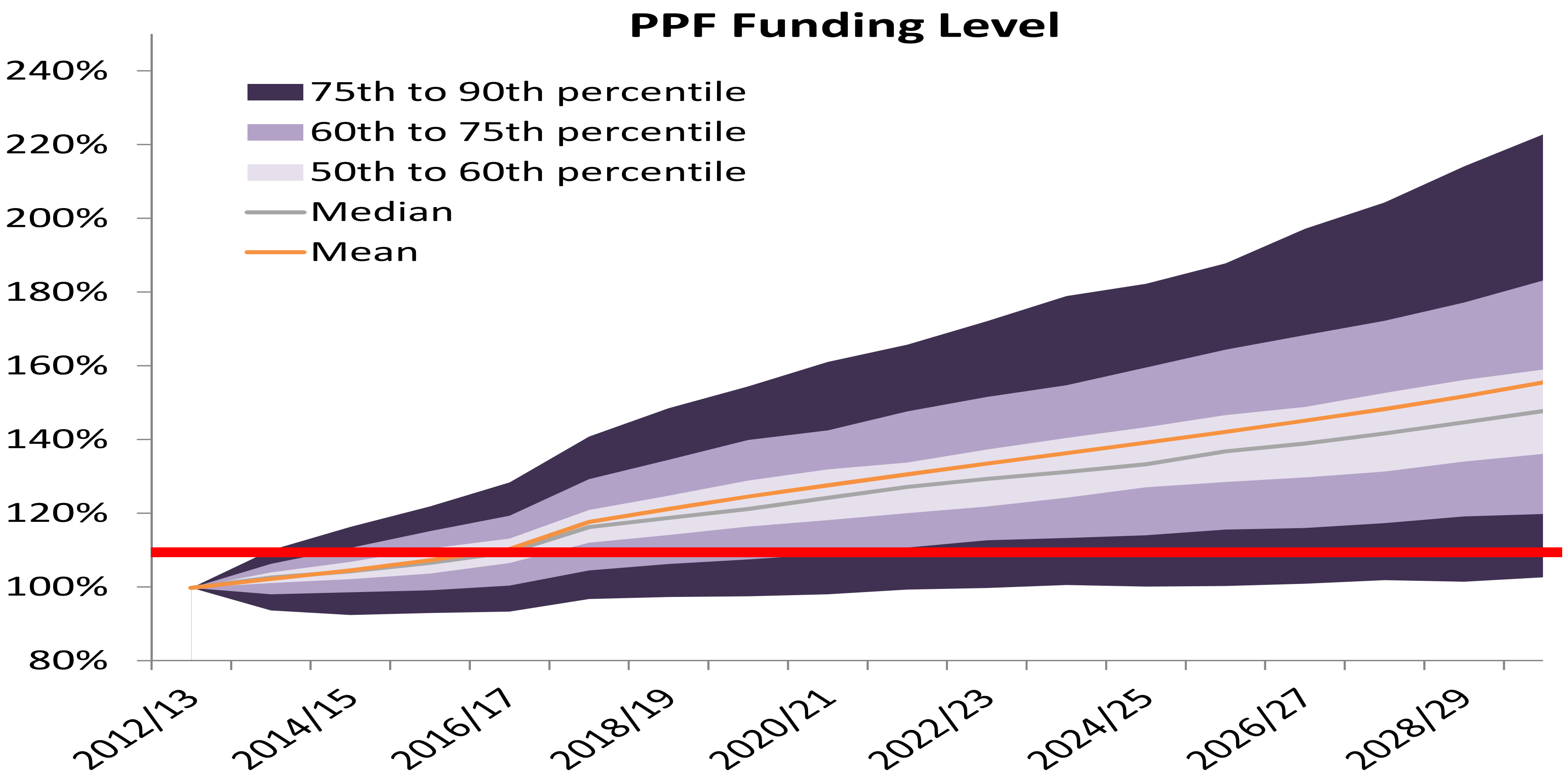
The PPF’s funding strategy

- 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?

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. This was 84% in March 2012.
  - downside risk: the 90% percentile of projected PPF deficits over the period to 2030. This was £10bn in March 2012.

The PPFs funding objective



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
- 2013/14 PPF levy: set at £630m, below £687.5m limit
- Potential changes to RPI formula
- Probability of success was 84% in March 2012, fall from 87% last year

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

Stress tests

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

A reminder on the New Levy Framework

- 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

A reminder on the New Levy Framework

- 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.

2012/13 levy

- Initial estimate for 2012/13 levy, given in late 2011, was £550m
- Based on an estimate of how conditions would be at 31 March 2012
- We now expect to collect around £630 million
- Higher than the initial estimate by £80m
- Due to fewer than expected type A contingent assets, fewer than expected deficit reduction certificates, and lower than expected yields.

Contingent Assets experience in 2012/13

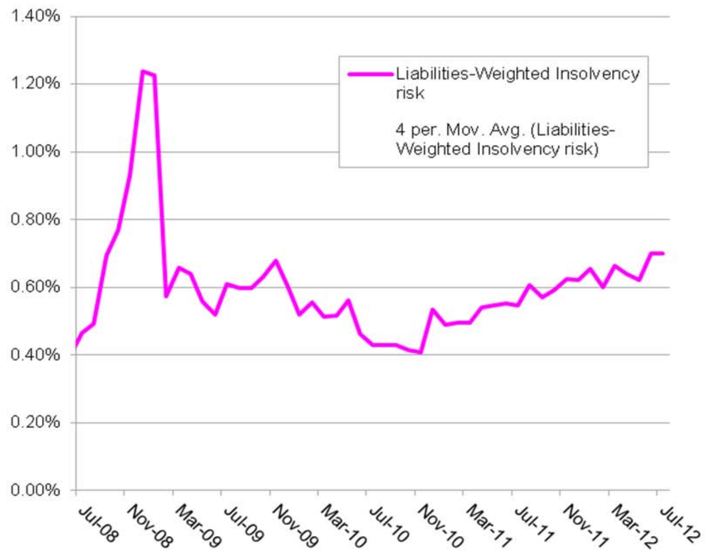
- Levy estimate assumptions for Contingent Assets:
  - re-certifications reduce levy quantum by c.£220m
  - New Contingent Assets reduce levy quantum by c.£40m
- Experience in 2012/13 differs significantly from assumptions:
  - value of re-certifications down 15% or c.£30m
  - value of new guarantees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

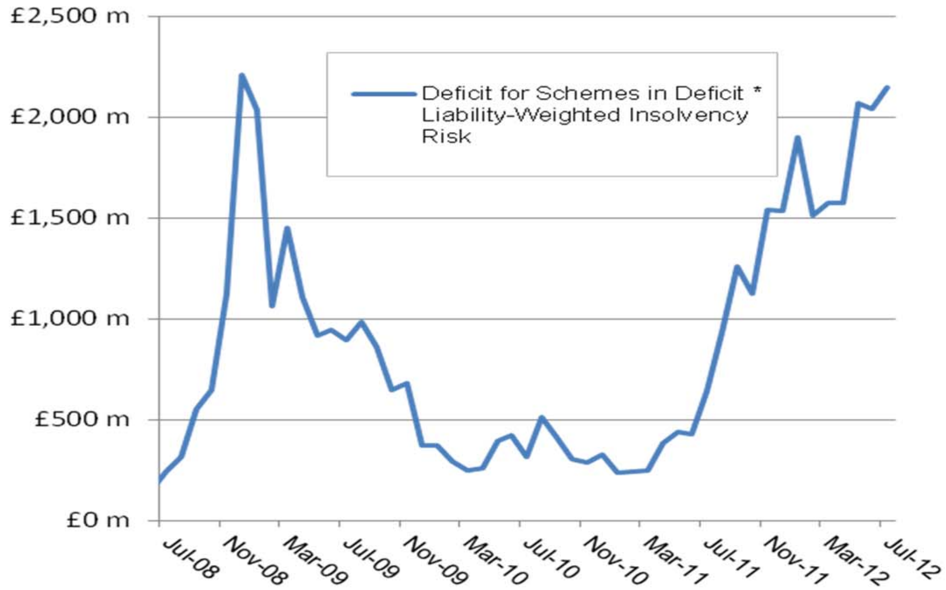
Type	11/12	Re-certified	New for 2012/13	Total 12/13
A	785	589 (including 61 modified)	157	746
B	117	99	30	129
C	17	6	2	8

2012/13 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.

2013/14 levy - PPF risk has risen sharply

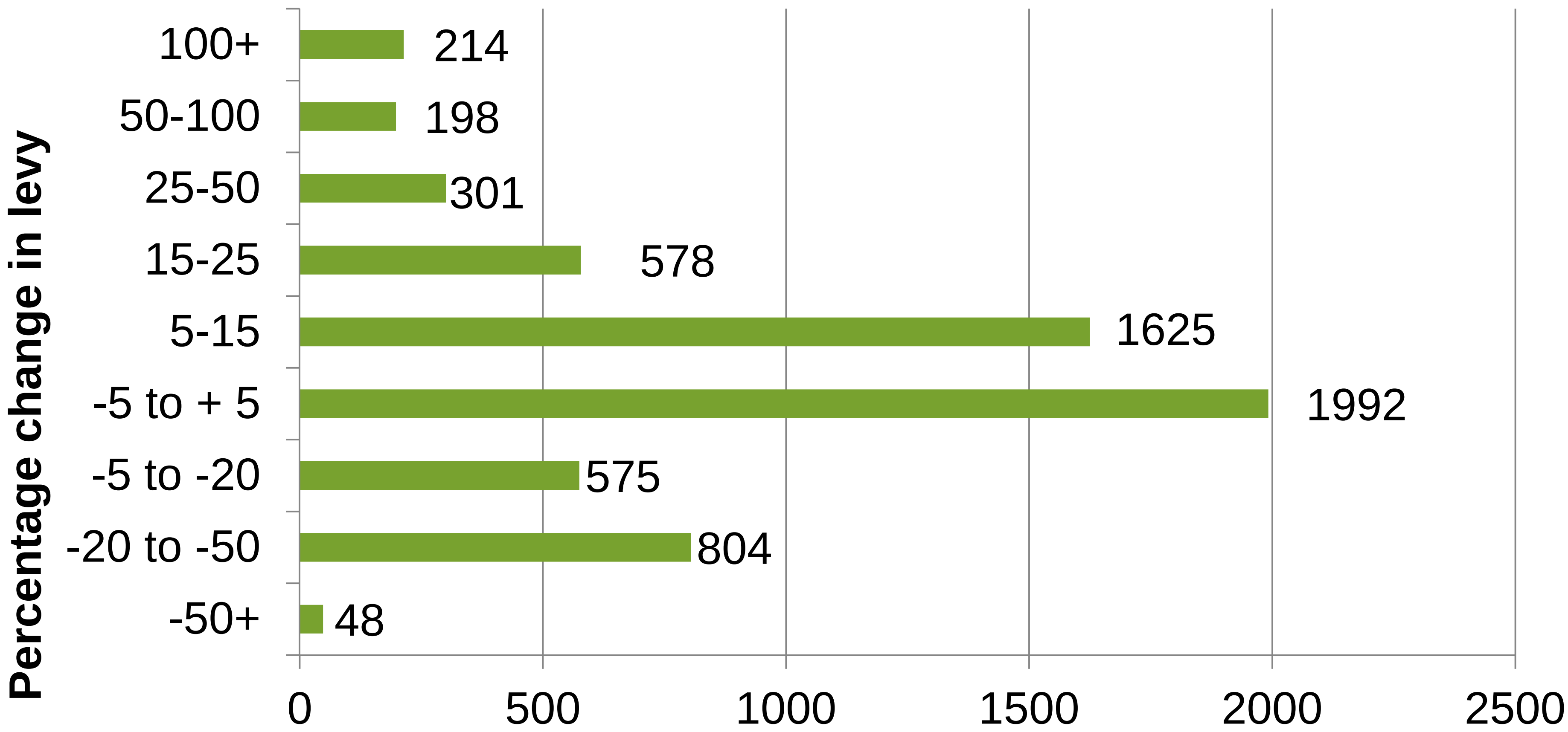




2013/14 levy proposal

- Would have collected £765m for 2013/14 had we used same parameters as for 2012/13
- Breaches upper limit of £687.5m (£550m + 25%)
- Board settled on £630m as estimate for 2013/14
- No increase compared with estimated collection for 2012/13

Projected levy impact: 12/13 vs 13/14



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 at £630m for levy year 2013/14, but the year after a 10% increase is likely without a change in markets

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 presenters.