

# London Borough of Harrow Pension Fund

2016 valuation – initial whole fund results

- Gemma Sefton
- 6 September 2016

# 2016 progress report



Event	Timescale	Progress
Assumptions agreed with Pensions Committee	21 June 2016	
Data received and cleansed	June/July 2016	
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# What are we going to cover?



Recap of steps to date



Valuation results



Next steps

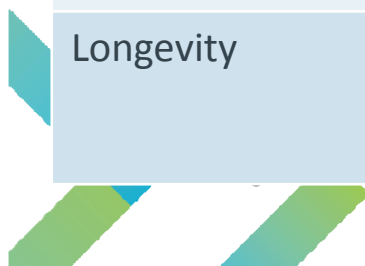


# Steps to date

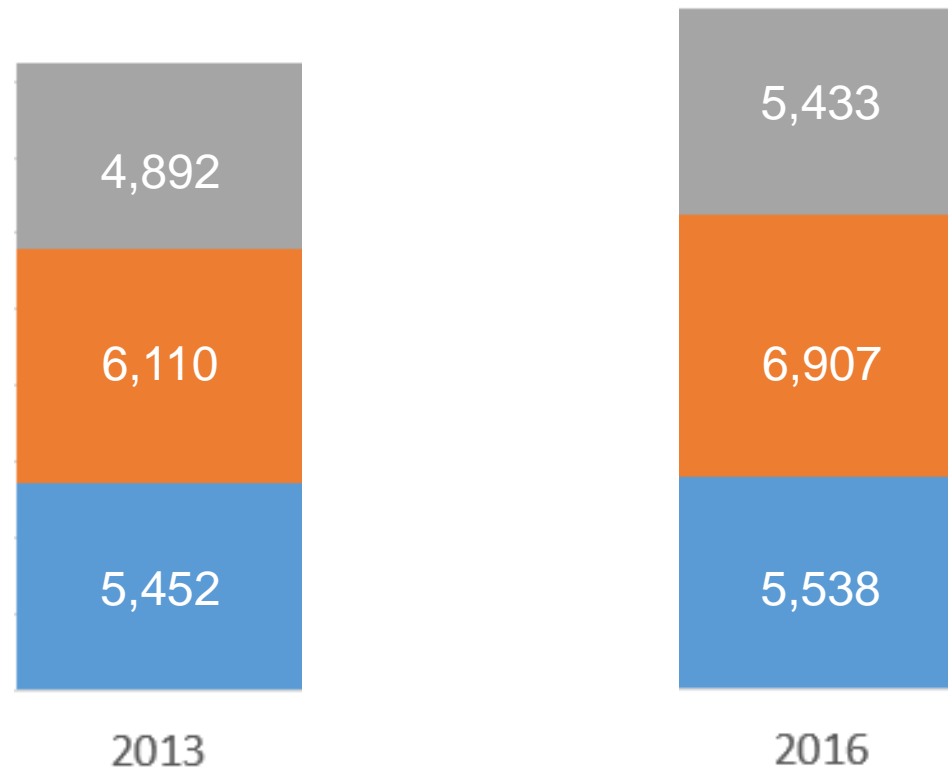
# Key assumptions for funding target



	2013 valuation	2016 valuation	Derivation of assumption
Discount rate (assumed future investment return)	4.6%	3.8%	No change in approach: Gilts plus prudent asset out-performance assumption (AOA) At 2013: AOA = 1.6% p.a. At 2016: AOA = 1.6% p.a.
Long term pay growth	3.8%	2.5%	Change in approach: At 2013: RPI + 0.5% At 2016: RPI – 0.7%
Pension increases (CPI)	2.5%	2.1%	Change in approach: At 2013: CPI = RPI - 0.8% At 2016: CPI = RPI - 1.0%
50:50 take up	10%	5%	Lower than anticipated take up
Longevity	Bespoke fund analysis, peaked improvements, CMI 2010 model for future improvements	CMI 2013 for future improvements	2013 to remove volatility experienced in last two years



# Membership data received and validated



■ Actives ■ Deferred pensioners ■ Pensioners



# Whole fund results

# Whole fund valuation results



	31 March 2013	31 March 2016
Active	293m	275m
Deferred	133m	171m
Pensioner	360m	444m
<b>Total liabilities</b>	<b>786m</b>	<b>889m</b>
Assets	552m	661m
<b>Deficit</b>	<b>(234m)</b>	<b>(228m)</b>
Funding level	70%	74%

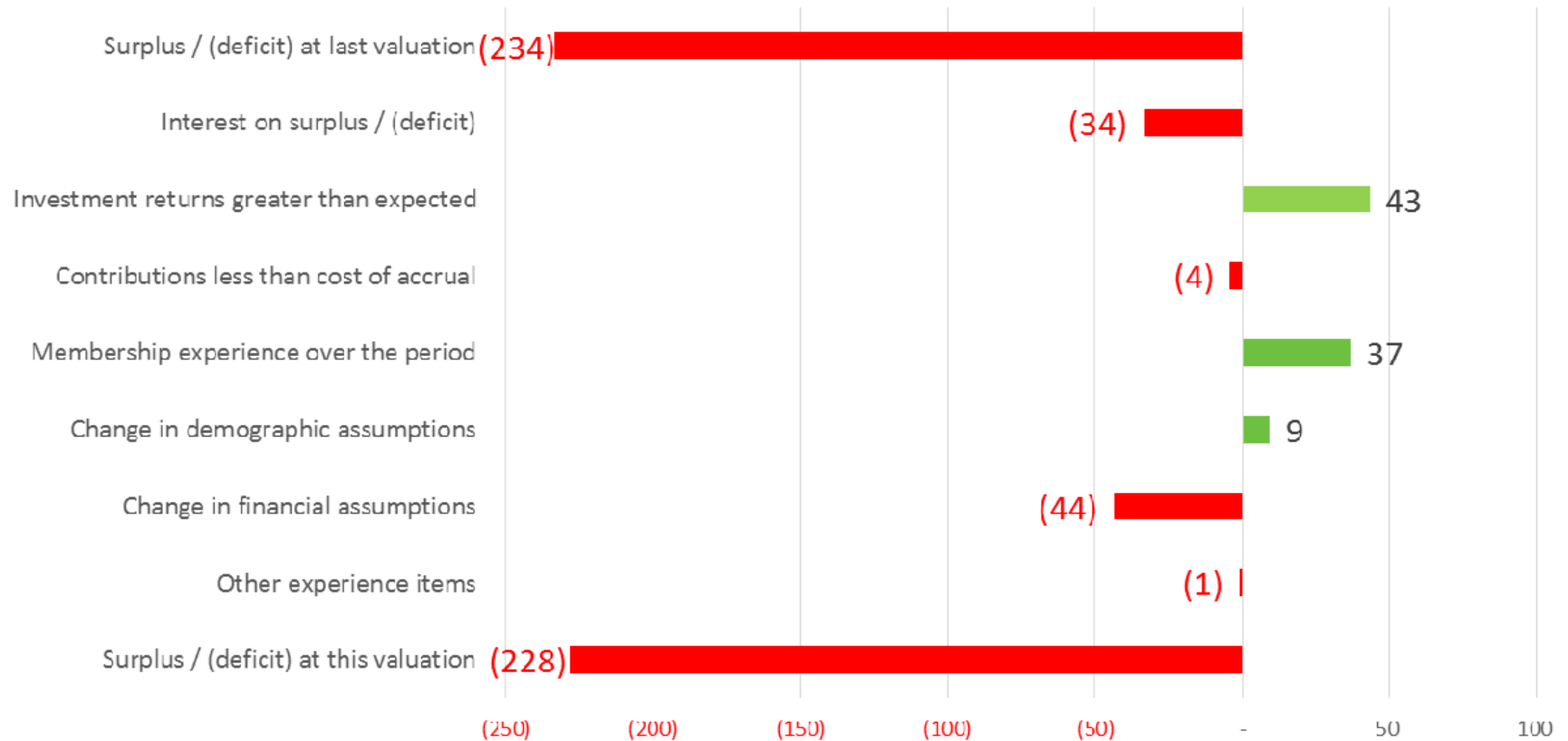
Deficit has fallen slightly in cash terms





# Why has the funding position changed?

Analysis of Surplus/(Deficit) from 2013 to 2016



# Membership experience

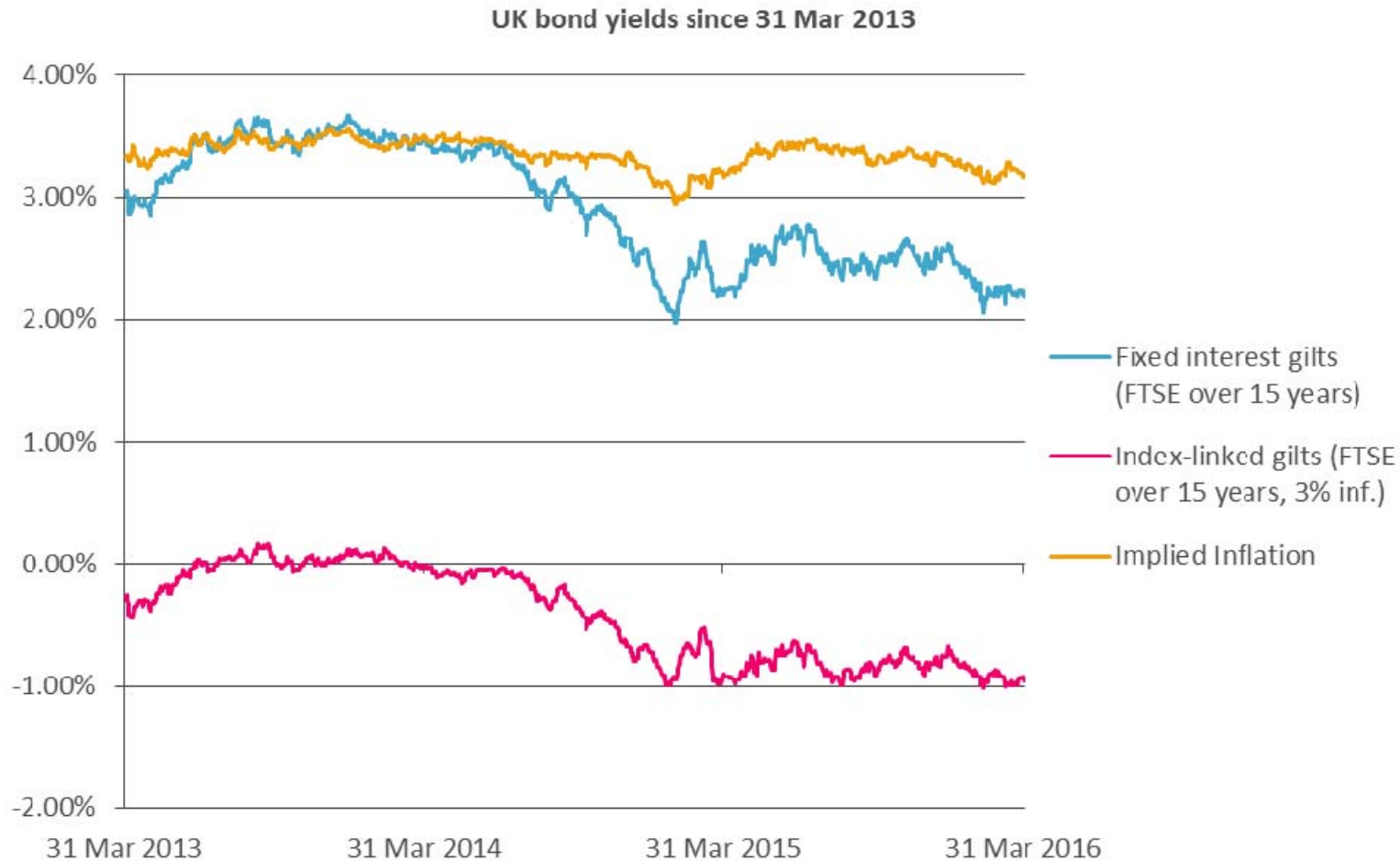


- **Pay growth**
  - Lower than expected
  - Does vary across employers
- **Pension increases** (pension increase orders)
  - Expected 2.5% p.a. (7.7%)
  - Actual 2.7%, 1.2%, 0.0% (3.9%)
- **Movements**
  - Fewer ill health retirements than expected
  - Fewer early leavers than expected
  - Fewer pensioner deaths than expected
- **50:50 take-up**
  - Lower than expected

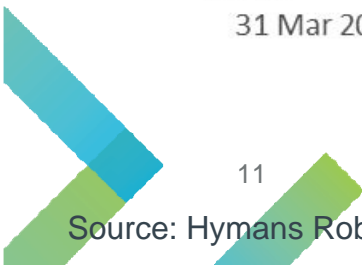


Details, not the headlines

# Experience since 2013



Falling bond yields have increased liabilities...



# Experience since 2013 (cont.)



Actual vs expected investment returns from 2013 to 2016



...but asset returns have been stronger than expected



# Outlook for financial markets



- Yes to
  - Heightened uncertainty and
  - Increased Sterling volatility

## **BUT....**

- Many concerns pre-date the Brexit result

*“Economic growth in the developed world since the Financial Crisis has been slower than at any comparable period except the Great Depression” GMO, 2016*

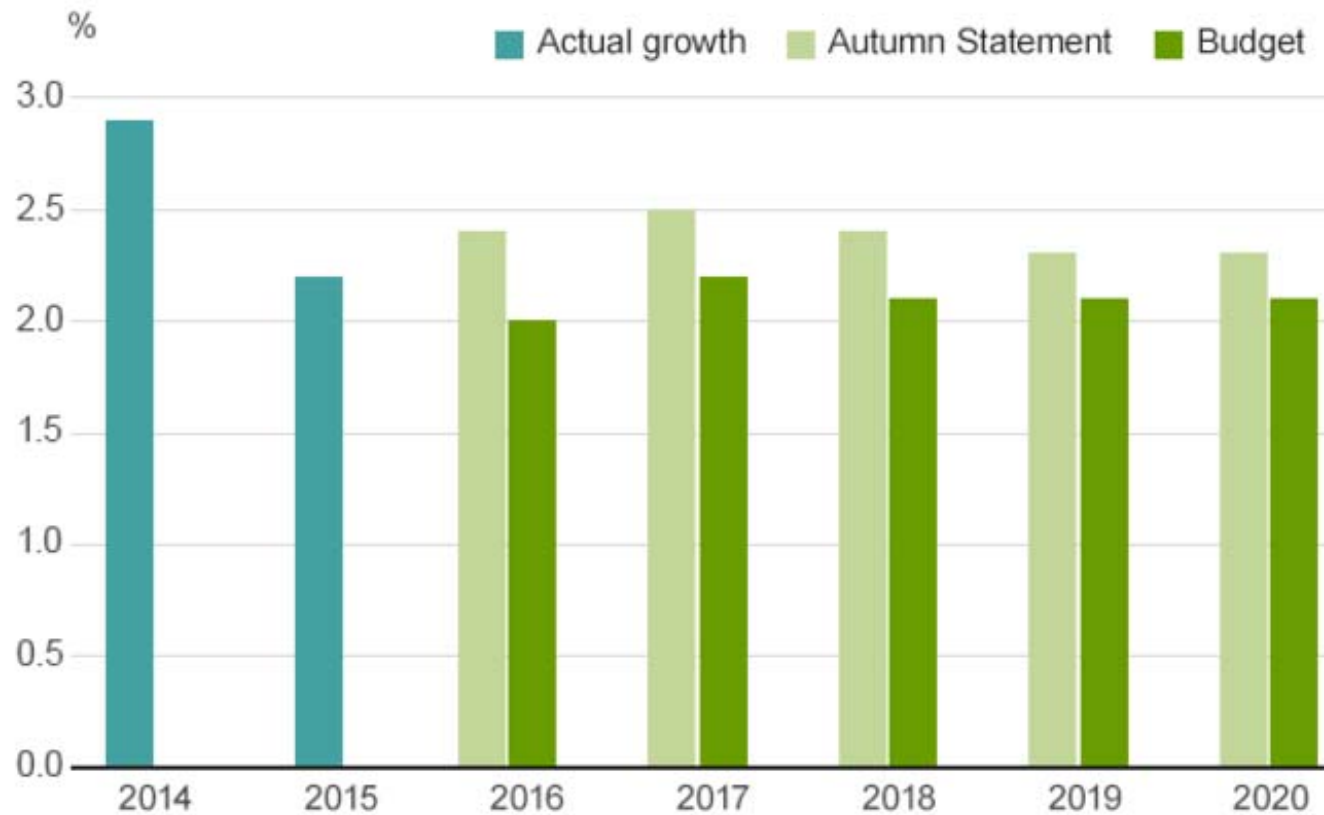
- OBR growth forecasts cut in Spring budget 2016



# Lower expectations for growth



**GDP growth forecasts**



Source: ONS and OBR



# What does this mean for asset returns?



“Projected return forecasts for 2016 – 2026 have fallen for developed market government bonds, investment grade credit, high yield bonds and global equity markets”

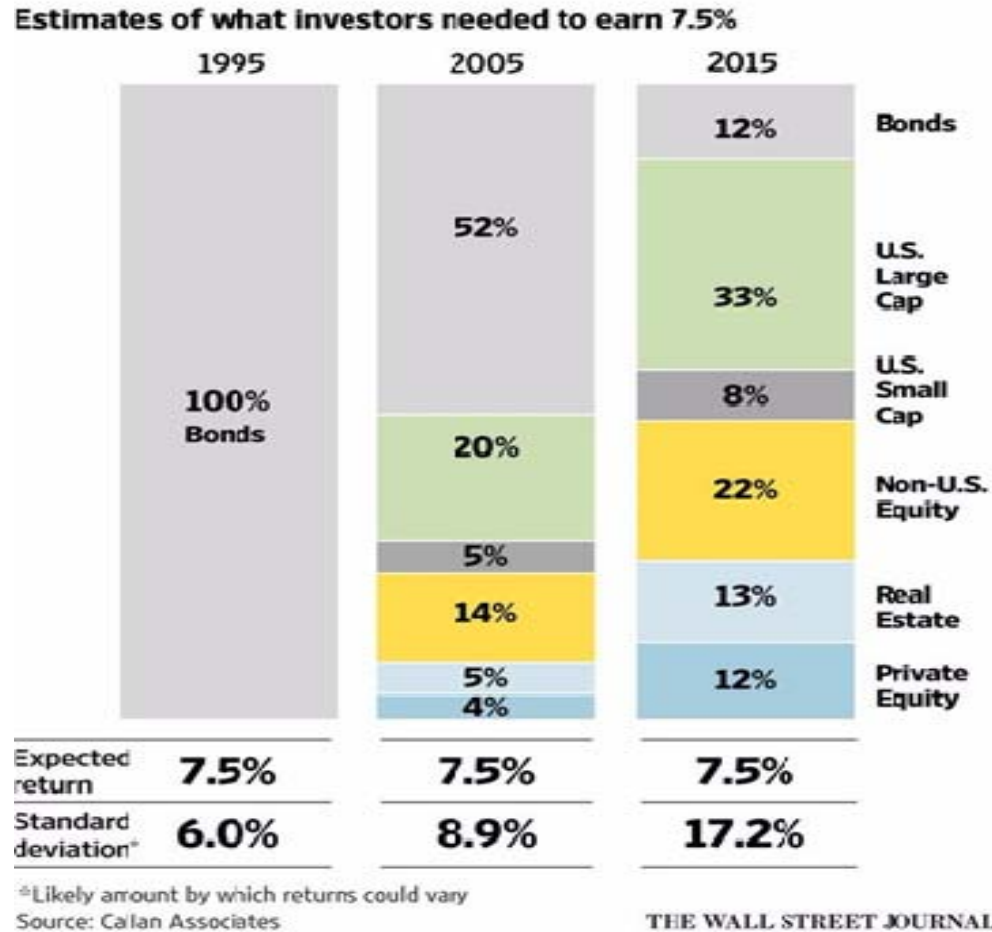
Baillie Gifford, 2016

“Our 2016 assumptions anticipate a challenging investment environment as policy and economic conditions globally continue to diverge and many asset returns fall short of those achieved over the past 30 years.”

JP Morgan 2016



# What this means for investors (example)



More risk needed to generate the same returns



# Next steps

# Setting employer contribution rates

Understand employers



What is their funding target?

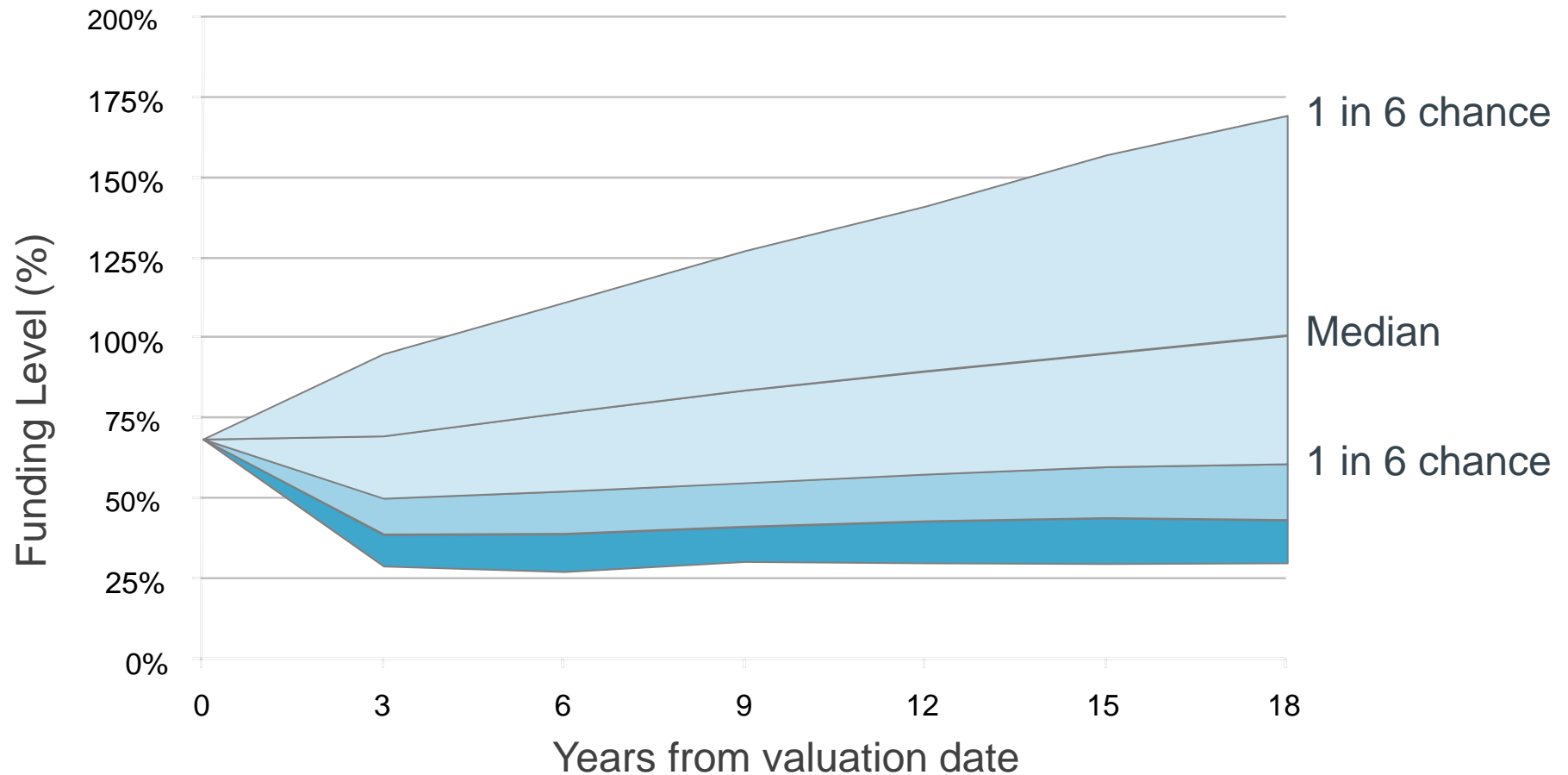


How long do we want to give each employer to get to the target?



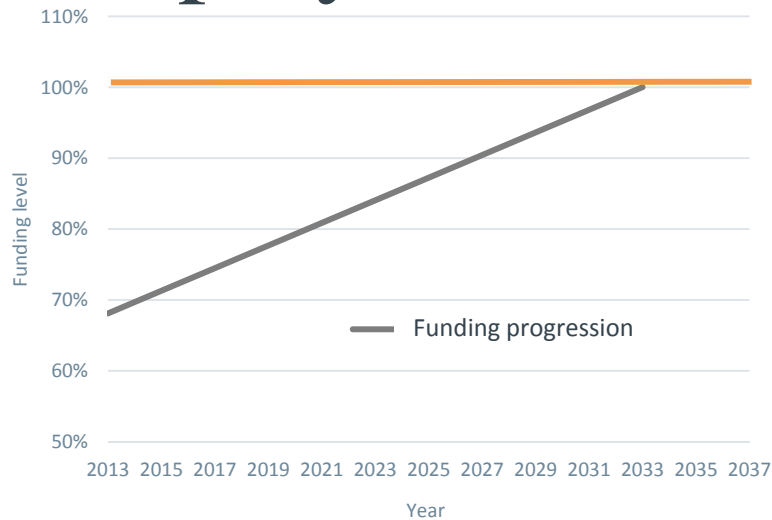
How much risk can each employer take to hit the target?

# Setting contribution rates: Harrow Council



Need a good change of meeting funding objective to be prudent

# Setting contribution rates: other employers

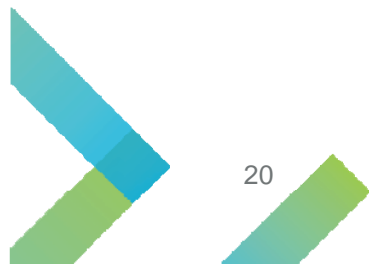


## The 'old' world

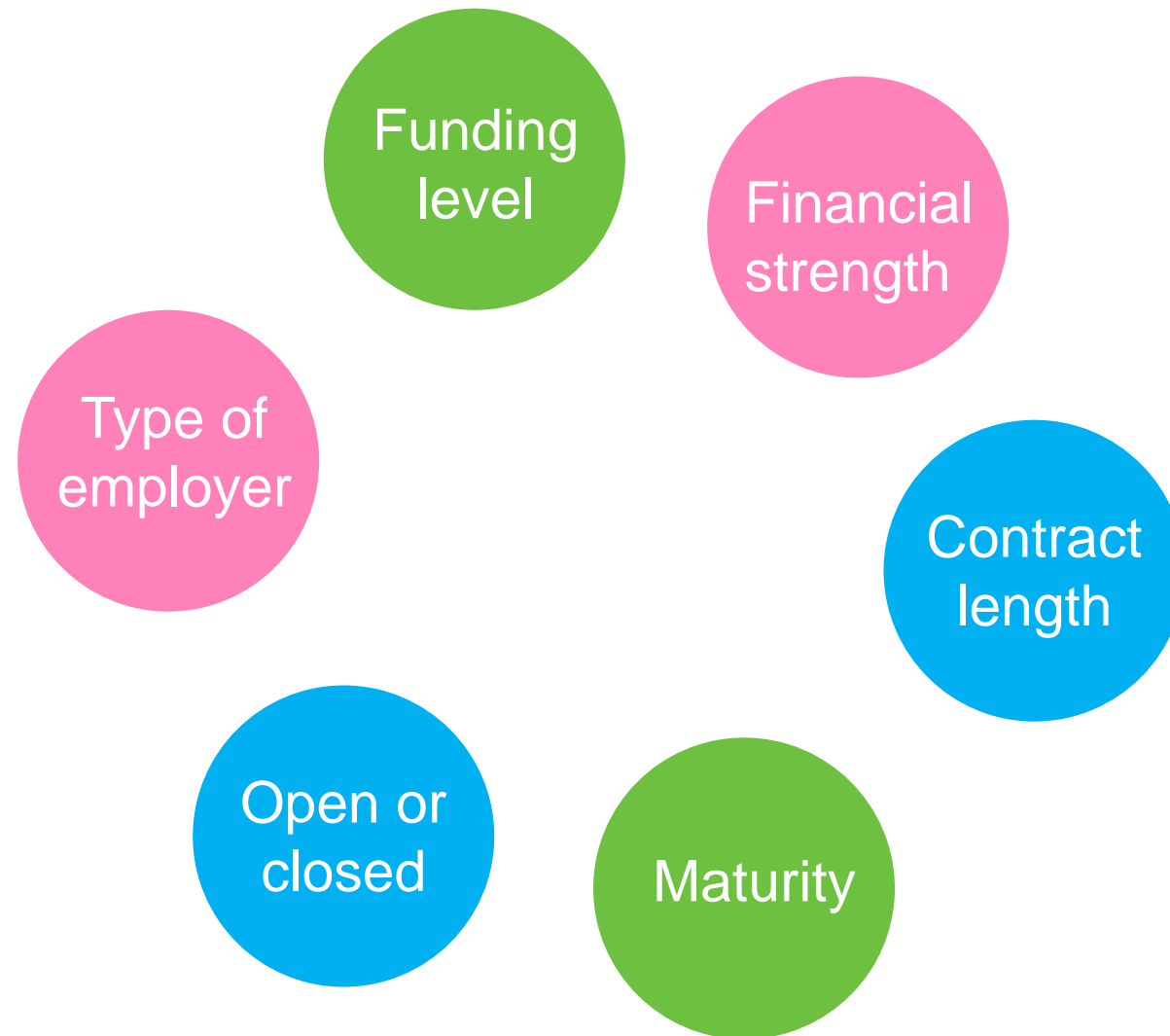
**Risk based contribution rate strategies set for all**

## The 'new' world

CONTRIBUTION STRATEGY	LONG TERM LIKELIHOOD OF SUCCESS	AVERAGE OF THE WORST 5% OF FUNDING LEVELS IN 2035
Strategy 1	58%	39%
Strategy 2	77%	55%
Strategy 3	67%	45%



# Recognising all employers are different



# Funding Strategy Statement review

## 3.3 The different approaches used for different employers

Type of Employer	Scheduled Bodies		Community Admission Bodies and Designating Employers		Transferee Admission Bodies
Sub-type	Council Pool	Academies	Open to new entrants	Closed to new entrants	(all)
Basis used	Ongoing, assumes long-term Fund participation (see <a href="#">Appendix E</a> )		Ongoing, but may move to "gilts basis" - see <a href="#">Note (a)</a>	Ongoing, but may move to "gilts basis" - see <a href="#">Note (a)</a>	Ongoing, assumes fixed contract term in the Fund (see <a href="#">Appendix E</a> )
Future service rate	Projected Unit Credit approach (see <a href="#">Appendix D – D.2</a> )		Projected Unit Credit approach if open (see <a href="#">Appendix D – D.2</a> )	Attained Age approach (see <a href="#">Appendix D – D.2</a> )	Projected Unit Credit approach if open, Attained Age otherwise (see <a href="#">Appendix D – D.2</a> )
Stabilised rate?	Yes - see <a href="#">Note (b)</a>	Yes - see <a href="#">Note (b)</a>	No	No	No
Maximum deficit recovery period – <a href="#">Note (c)</a>	20 years	20 years	15 years – subject to security / covenant check	15 years – subject to security / covenant check	Outstanding contract term
Deficit recovery payments – <a href="#">Note (d)</a>	Monetary amount	Monetary amount	Monetary amount	Monetary amount	Monetary amount
Treatment of surplus	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Preferred approach: contributions kept at future service rate. However, reductions may be permitted by the Administering Authority		Reduce contributions by spreading the surplus over the remaining contract term
Phasing of contribution changes	Covered by stabilisation arrangement	Covered by stabilisation arrangement	None	None	None
Review of rates – <a href="#">Note (f)</a>	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations				Particularly reviewed in last 3 years of contract
New employer	n/a	<a href="#">Note (g)</a>	<a href="#">Note (h)</a>		<a href="#">Notes (h)&amp; (i)</a>
Cessation of participation: cessation debt payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt		Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation – see <a href="#">Note (i)</a> .		Participation is assumed to expire at the end of the contract. Cessation debt (if any) calculated on ongoing basis.

# Contribution rate definitions



- **Primary Contribution Rate**
- This refers to the cost of new benefits being earned by members. This was previously referred to as the Future Service Rate.
- **Secondary Contribution Rate**
- This refers to the contributions required to repair an employer's deficit (surplus). This was previously referred to as Deficit Recovery Contributions





HM TREASURY



Public Service Pensions  
(Record Keeping) Regulations

The Pensions  
Regulator

Governance and administration of  
public service pension schemes



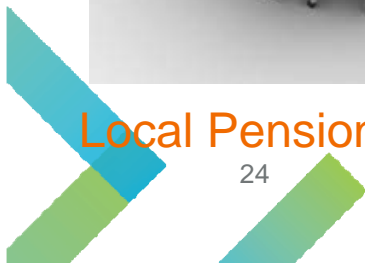
Local Pension Board



Scheme Advisory Board



HYMANS  ROBERTSON

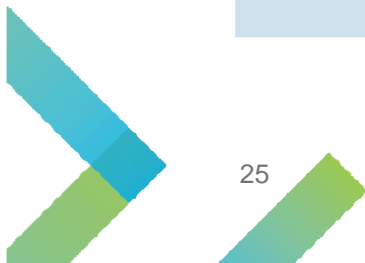




# The two “regulators”



Regulator	SAB	DCLG (GAD)
Powers?	Influence	Statutory
Request valuation info by	30 Sep 2016	Q2 2017
What requested?	Basket of Key Performance Indicators	Different Key Performance Indicators
Actuarial basis	HMT	Different
Publish results?	Possibly, in Q3 2016	Probably, in mid-2018



# Whole fund valuation results – SAB basis



	31 March 2016 (funding basis)	31 March 2016 (HMT basis)
Active	275m	221m
Deferred	171m	128m
Pensioner	444m	377m
<b>Total liabilities</b>	<b>889m</b>	<b>726m</b>
Assets	661m	661m
<b>Deficit</b>	<b>(228m)</b>	<b>(65m)</b>
Funding level	74%	91%

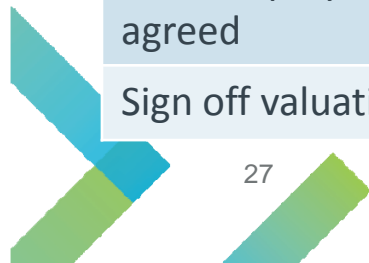
Funding basis is deliberately prudent – GAD have noted  
HMT basis isn't suitable for funding purposes



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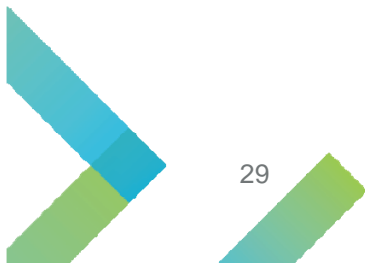
Thank you

# Reliances and Limitations



- This presentation is addressed to the Pensions Committee of the London Borough of Harrow Pension Fund for its sole use as Administering Authority and not for the purposes of advice to any other party; Hymans Robertson LLP makes no representation or warranties to any third party as to the accuracy or completeness.
- This presentation discusses the current issues in the LGPS and was prepared purely for illustration to employers. Hymans Robertson LLP accepts no liability for any other purpose of this presentation.
- The following Technical Actuarial Standards\* are applicable in relation to this presentation and have been complied with where material:
  - TAS R – Reporting;
  - TAS D – Data;
  - TAS M – Modelling; and
  - Pensions TAS.

\* Technical Actuarial Standards (TASs) are issued by the Financial Reporting Council and set standards for certain items of actuarial work, including the information and advice contained here.



# Appendix

# Results are sensitive to assumptions about the future



## Financial assumptions

Benefit Increases					
Discount Rates		2.0%	2.2%	2.4%	
	4.0%	(179) 79%	(204) 76%	(229) 74%	(Deficit) Funding Level
	3.8%	(203) 76%	(228) 74%	(254) 72%	(Deficit) Funding Level
	3.6%	(228) 74%	(254) 72%	(280) 70%	(Deficit) Funding Level

## Demographic assumptions

	Peaked improvements	Non-peaked improvements
(Deficit)	(228)	(249)
Funding Level	74%	73%

