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Pensions Age Northern Conference: Hitting the target

A year on from the inaugural conference, the subject has moved on from what may happen if the UK votes for Brexit, to how pension funds can continue to hit targets regardless of the UK's departure from the EU. Delegates were treated to a range of talks from experts across the pensions industry

The backdrop to the second Pensions Age Northern Conference was much like the first, the nation tasked with another political vote that could change the trajectory of the country.

However, despite taking place the day before the General Election, the dialogue centred very little on the political backdrop; instead, pensions were very much at the forefront, with minds' focused on hitting targets.

Industry bodies

The day began with an update from the Pension Protection Fund, which its chief risk officer, Hans den Boer noted has experienced "greater focus" over the last two years due to high profile cases such as BHS, Tata and Hoover.

"In all cases, we are there to provide protection and there is no doubt we are in a good financial position and we can afford to pay compensation to members."

Den Boer also talked about the renewed focus on defined benefit pensions, with the publication of the government's green paper last year. He said the PPF believes the defined benefit system is not broken and most members will get the pensions they were promised. He also said he was uncomfortable with the phrase "dumping" to describe when a scheme falls into the lifeboat fund.

Also on the subject of the PPF, Rothesay Life head of business development team Sammy Cooper-Smith, said many people do not realise how bad the true value of compensation from the PPF is.

"The PPF is a lot better than what went before, but when you look at the value of someone's pension if they're subject to PPF cuts, they can lose between 10 and 50 per cent of their benefit.

"It's engineered such that they don't see a big cut on day one, and for those that don't understand inflation and pension increases it doesn't look very bad. But in terms of the true value of their benefit if it goes into the PPF, there is a significant reduction," he said.

Another of the conference's keynote speakers was The Pensions Regulator's head of policy, Fiona Frobisher. She noted the regulator is changing to be clearer, quicker and tougher, as a result of recent scrutiny due to the high profile Work and Pensions Committee case on BHS. Talking more generally about pensions, Frobisher said auto-enrolment has been a success but said defined benefit schemes are on more of a "bumpy road". She stressed defined benefit schemes should carry on and hope that things get better.

Pensions administration

On the subject of pensions administration, JLT Employee Benefits director Mark Adamson spoke about the three pillars of service; process, people and technology. "If administrators are getting those three pillars right

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then they have a decent chance of actually delivering a good service to members, trustees and employers.

For example, he said from a process point of view it is important that administrators "constantly challenge what they are doing and why they are doing it". In terms of people, it is necessary that people are trained properly and treated appropriately. In terms of technology, he said it is key to pension administration.

Barnett Waddingham partner and head of workplace health and wealth Damian Stancombe, with the aide of the firm's *Generation, Why?* survey looked to help delegates understand how different cohorts, based on age, affluence, location and gender, view money matters, and how they can re-engage them to reach their goals.

"When we actually look at Generation Y, and what the results are saying, pensions are not that high up. People are sitting there, aged 18-29, saying my issue is the property ladder. We have created this illusion in the country that property is the be all and end all… People are trying to save for a house, struggling with debt and you're ramming down their throats that a pension is really important to them," he said.

De-risking

LCP partner Ken Hardman talked to the audience about reducing risk using buy-ins, buyouts or longevity swaps. On the subject of de-risking effectively he listed three key principles; measure longevity risk alongside your other investment risks; choose a buy-in or longevity swap, dependent on your investment risk appetite; and consider the implications of your broader journey plan.

He gave an example of the £3.5 billion Philips Pension Fund that, through four buy-ins, led to a full buyout. In 2011, it was a mature scheme with 66 per cent of its members retired. It was around 90 per cent funded on a gilts basis but the longevity risk was becoming significant. It completed its first buy-in in August 2013 with Rothesay Life for £484 million, a £300 million buy-in followed with Prudential in June 2014 and a further £300 million in September 2014 with Prudential. The final buy-in took place in November 2015 with the Pension Insurance Corporation for £2.4 billion.

Investment

Investment was a popular topic throughout the day and UBS director of UK and Ireland institutional Rachel Hill spoke on the issue of climate change, noting the Paris Agreement, which has strengthened the global commitment to tackling climate change by aiming to limit earth's temperature increase to two degrees each year. However, she described climate risk as a "long-term structural problem" that she said has been noted by Nest. The provider has now implemented low-carbon solutions within its portfolio after partnering with UBS. She explained that exclusion has traditionally been the investment policy used by Nest but this did not allow the fund to engage at a corporate level.

"Rather than excluding, we were able to work with them to assess qualitative and quantitative factors to help us provide tilts in the portfolio by overweighting and underweighting the constituent parts of the index using these factors," she explained.

Changing topic, Kames Capital indirect property fund manager Tony Yu, spoke to the audience about investing in property. He noted that investing in property has its challenges; it is impossible to create a passive index, there are issues of scale, high transaction costs and it is an illiquid asset class but it offers good long-term returns. However, the question should not be why you invest in property but how. Yu said there is "no simple answer" but it can be accessed through a direct portfolio, multi-manager funds, derivatives, balanced funds or a real estate investment trustee among others.

Challenging the idea of reducing risk in a portfolio was Pictet Asset Management head of international multi-asset Percival Stanion. He stated that currently there are no cheap asset classes available, and traditional low-risk assets such as bonds and cash are "terrible value

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for money". However, he noted there are "some pockets of value in equities" and he also suggested UK real estate, which is "not a fantastic asset but it is probably going to be better than bonds".

"I have been telling clients that if they can stick with pure equities, they should do so. Unfortunately for them, very often the decision has been taken at a higher level that the pension needs to be de-risked and they have already decided they're going down a multi-asset approach. If you have the longer investment horizon, if you have the governance budget for it, you should stick with equities," Stanion added.

Schroders fiduciary manager Hannah Simons talked about a new acronym within pensions, which is cashflow driven investing (CDI). Its key features include having a higher yield than pure matching assets; greater certainty of outcome than traditional growth assets (but less scope for upsides); and, it is low maintenance and a stable funding level through time.

"Essentially CDI incorporates corporate bonds into those matching assets and this allows you to do is deliver a slightly higher return than those pure matching assets provide. One of the key benefits of adopting a CDI approach is that the investment in corporate bonds provides a much more certain return of capital than we get from other traditional asset classes that we've invested in," she said.

AXA Investment Managers head of UK LDI Jonathan Crowther stressed what a challenging time it is for pension schemes. Despite strong asset returns, falling yields have hurt scheme funding levels. As a way round this, he said schemes should avoid forced selling by appropriately structuring credit assets to reduce costs. Crowther added that by integrating credit and LDI it is possible to further improve overall efficiency.

J.P. Morgan asset management managing director Robert Hardy explored the current themes and trends in infrastructure and how by focusing on deal flow and implementing platform investment strategies you can find value in a competitive market. He noted that core infrastructure discount rates have decreased approximately 30 per cent since 2000 and they have declined in line with the risk free rate.

RBC GAM Global Equity senior portfolio manager Ben Yeoh spoke to delegates about how integrated ESG adds value. "Not everything that counts can be counted and not everything that's counted, counts," he said. He explained that this means a company is more than just its numbers, it has various stakeholders.

"If you don't take care of one of those stakeholders, it comes back to bite you and this is the idea of integrating non-financial types of information into your assessment of a company." He noted that a company with strong ESG values creates healthier overall capital, leads to more sustainable businesses and ultimately delivers superior financial results.

Vontobel Asset Management head of UK and Ireland Sheridan Bowers looked at how pension schemes should go "back to basics" and look at how they can work their equities harder to generate a better return. "We believe that if you take a long-term approach you can generate significant outperformance over the full market cycle. Therefore, we believe that winning over time is not necessarily the same as winning all the time." Bowers also noted that for a pension scheme "time is your greatest ally".

To conclude, he said he thinks equities still have a very important place within portfolios of defined benefit and defined contribution schemes. "With low rates expected over the next decade or so, working your assets harder will help schemes achieve the growth they require and actively managed equities can deliver long-term value for pension scheme investors."

Written by Natalie Tuck