New targets

John Baines and Alastair McIntosh explore how, for the first time ever, more schemes are targeting buyout than self-sufficiency

Over the past decade, Aon's *Global Pension Risk Survey* has charted the long-term ambitions of UK defined benefit (DB) schemes. During that period, we have seen a consistent increase in the number of schemes aiming to buyout – but our 2021/22 survey marks a significant tipping point.

For the first time this year, the number of schemes targeting buyout (47 per cent) is greater than those aiming for self-sufficiency (34 per cent). Improvements in schemes' funding positions have made buyout more achievable, alongside a continued appetite for risk reduction and increasing scheme maturity.

In 2019, participants expected to take an average of 9.4 years to reach their target, but in our 2021/22 survey, this has reduced to just 8.8 years. By the end of the 2020s, the average pension scheme will have reached its goal, driving a significant change in the UK's DB landscape.

Increased appetite and compacted timescales for buyout are significant for insurers and schemes alike. The buyout market has been relentlessly busy for insurers across the past five years. Annual transaction volumes have tripled in that time, and there is no sign of a slowdown in insurers' growth ambitions.

A further increase in buyout activity is sure to put strain on an already busy market. The robustness shown to date should give schemes of all sizes confidence that they can find attractive pricing and good terms in the market. However, insurers may become more selective when volumes of business are high or when a major, multi-billion pound transaction comes to fruition, so schemes will need to consider this when developing their strategy.

Well-prepared schemes are attractive to insurers and will be able to take advantage of market opportunities as they occur. Good quality decision-making and credible flightplans are indicators that schemes are taking long-term planning seriously. Our survey found that 52 per cent of schemes believe their flightplan is robust, with just 9 per cent describing it as 'aspirational', a fall from 16 per cent in 2019.

Schemes intend to reach their long-term target primarily through asset performance (63 per cent), sticking to their agreed funding plan (54 per cent) and increasing maturity (33 per cent). Beyond investment and contributions, there are other activities that schemes will need to prioritise in order to prepare for buyout.

Understanding and managing longevity risk – This will become more important as schemes get closer to their long-term targets. Almost half (48 per cent) of schemes have not yet considered hedging longevity or do not expect to do so. Other concerns, such as interest rate and investment risks, may have distracted from longevity risk in previous years, but schemes will need to prioritise longevity now, as buyout timelines shorten.

Member options exercises – Over a quarter (28 per cent) of respondents said that they expect to carry out exercises such as pension increase exchanges (PIE) or bulk transfer value exercises as part of their flightplan. That is nothing new, but the way in which schemes perceive member options exercises is changing. Rather than a standalone activity, they are now interlinked with other long-term activities such as GMP equalisation.

GMP equalisation – this continues to be a major, long-term project for schemes. While it is not directly related to specific long-term targets, the outcomes of GMP equalisation, such as better-quality data, can also help schemes make progress towards buyout. In our 2021/22 research, no respondents had completed their GMP equalisation exercise, but many had made good progress in areas such as decision-making structures (62 per cent).

Data cleansing – Good quality, clean data is a core component of buyout preparation. It is a clear signal to insurers that a scheme is taking buyout preparation seriously, as poor-quality data can affect everything from member communication to transaction pricing. Schemes might decide to address data cleansing as part of buyout preparation specifically, or within wider plans, such as GMP equalisation. In our 2021/22 research, we saw that 49 per cent of schemes have addressed data gap analysis as part of their GMP equalisation plans.

The growth of buyout as a long-term goal in our research shows that schemes now believe this is genuinely achievable for them. To reach their target within their anticipated timescales, schemes will need to continue to build relationships with potential buyout partners and plan for activities which – alongside investment performance and funding plans – will take them ever closer to their target.

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