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Pensions Age Northern Conference

Now in its third year, *Pensions Age*'s northern conference is a well-established annual event for pension professionals in the north. Speakers ranged from The Pensions Regulator and Pensions and Lifetime Savings Association to NEST and LCP, as well as many more

Opening the conference with an update from The Pensions Regulator was its head of policy Fiona Frobisher, who listed the regulator's six key priorities: expanding regulatory approaches, good trusteeship, DB schemes, master trust schemes, auto-enrolment and Brexit.

Focusing on the latter, Brexit, she said that as a "quasi-government agency" there are areas of risk arising due to Brexit. "We're looking at three areas of risk," she said, with the first being the risk to schemes from economic issues that could occur because of Brexit.

"We are also considering the implications for us as an employer, as we are an employer of 600 people, some of whom are European nationals, so we need to figure out what that means for us," she added. Lastly, Frobisher said the regulator is having to look at what it means for legislation, highlighting the IORP II Directive, which is due to be implemented in 2019; she also highlighted the issue of cross-border pension schemes.

Furthermore, Frobisher said that the TPR Future programme is now on "fast forward" because TPR CEO Lesley Titcomb has announced her resignation. She noted that Titcomb has been a "driving force" behind changing the way the regulator approaches its role. Highlighting this, Frobisher noted the regulator's use of more powers, such as prosecuting employers that don't comply with auto-enrolment.

Another keynote speaker was the Pensions and Lifetime Savings Association's policy lead: engagement, EU and regulation, James Walsh, who spoke to delegates about the "fantastic ideas" to improve pensions communication. These include standardised pensions statements, the pensions dashboard and national retirement income savings targets. He stressed that everyone in the pensions industry needs to "get behind" the ideas to help improve the way the industry engages with people about their pensions.

Walsh explained how the three ideas are complementary: "If we are going to get people more engaged with pensions, we've got to give them more information in a way that they can understand – so that is simpler statements. If they're going to understand if they're saving enough for retirement, or if they need to save more, then that's where the targets will help them understand, and in order for the targets to work, you've got to pull together information about the entirety of people's pension entitlement, and that is the dashboard."

Adding to the diversity of the keynote speakers was the Trade Union Congress' pensions policy officer Tim Sharp, who said pensions inadequacy is central to the TUC's work around pensions, and at the very heart of the issue is that savers don't have a good understanding of what constitutes as pensions adequacy.

He noted that when we think about pensions adequacy we think about replacement rates, but he described it as a "pretty crude mechanism", as it suggests that we shouldn't worry about people who have spent their life on a low income being in poverty in retirement. He stressed that the TUC's view on pensions is that all workers should be able to enjoy a retirement free from poverty. Therefore, the TUC supports the creation of a permanent Pensions Commission, but Sharp was quick to highlight that it is not a "naïve expectation of taking politics out of pensions". He stated that important decisions will always be a matter for politics, but the previous Pensions Commission showed the "desirability of building consensus around potential reforms, so the reforms are longstanding".

Investment

Speaking to delegates about investment and the economy, Pictet head of multi-asset London, Andrew Cole, said that he doesn't think an economic downturn will happen anytime soon. "It has been a very long, slow, and ponderous economic recovery." However, he said we are in the middle of a very long economic cycle that will last around 15 years – noting that usually they are only every seven years.

For the past five years equities have constantly beaten bonds, Cole noted, and it is unlikely based on today's interest rates that bond returns will go up – and equity returns are not going down anytime soon. "We are in a period of financial repression, where governments are doing everything they can to replenish their bank sheet, and unfortunately, that typically comes at the cost of savers," he said. In addition, he said increased regulatory oversight is forcing pension schemes and insurance companies to own government bonds, which he said is an example of financial repression.

On the other hand, UBS asset management director Michael Walsh looked at why investors are rethinking their equity holdings, namely because of volatility in the markets. However, he said given economic growth is still strong, UBS still currently holds the view that equities are a better alternative to bonds or credit. "What we are looking at here is not selling out of equities, but thinking how you might hold an equity portfolio that avoids some of the sharp sting you may feel in a market downturn," he said.

There are two strategies, he said, a global income strategy focused on increasing expected income with less volatility, and a defensive equity strategy, which has more of an "explicit downside protection feature". It combines a global equity portfolio with a systematic hedging overlay.

Moving on to the subject of cashflow was J.P. Morgan head of EMEA pensions solution and advisory managing director Sorcha Kelly-Scholte, who highlighted that cashflow challenges can act as a drag on funding levels and increase volatility. She stated that three quarters of FTSE 350 companies have schemes that are in negative cashflow.

Scholte said pension trustees need to build their strategy: "Think as cashflow driven investing not just as something you do at the end of your scheme, you have to think about it today because you have negative cashflows today," she said.

When it comes to a cashflow-driven approach, she gave a breakdown of a portfolio; growth (7 per cent), real income (20 per cent), LDI (41 per cent), core (17 per cent) and core plus credit (15 per cent). She also noted that restricting to sterling markets limits opportunities and global markets offer greater depth at all durations.

AXA Investment Managers head of structuring and business development – external managers, structured finance, Pierre-Antoine Godefroy also highlighted the issues of being cashflow negative;

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he stated that 85 per cent of schemes expect to be cashflow negative over the next 10 years. Therefore, he spoke to delegates about investment opportunities across the credit continuum. He said that the total credit universe is worth $30 trillion, and is worth considering because it offers higher risk-adjusted yields. Schemes can also benefit from a rising rate environment, and the diversification of the growth portfolio to improve investment outcomes.

Defined benefit

LCP partner Ken Hardman addressed delegates on de-risking, focusing on insurer pricing for buy-ins and buyouts. He told delegates that last year there were around £18 billion worth of transactions, with £12 billion being buy-ins and buyouts and the remaining £3 billion being longevity swaps. In particular, he noted the "momentum" in the market with small- and medium-sized schemes also looking at de-risking options.

"We often compare the cost of a buy-in against the cost of investing in gilts," he noted. "What we have seen over the last couple of years, since the Brexit referendum, is a material improvement in pricing, meaning you can now lock into to asset returns of gilts plus 20-25 basis points, and that is one of the reasons that volumes have been increasing."

Linking back to the regulator's focus on governance, Schroders head of fiduciary management Hannah Simons noted that good governance is crucial to running a pension scheme. However, she stated that some tasks can be delegated, such as selecting asset classes, and managers.

"A trend that we have seen in the UK market over the past few years has been an increase in delegation. Different models have been adopted by different types of pension schemes, smaller schemes for example have used fiduciary management, and at the other end of the spectrum, in larger schemes we have seen a huge increase on in-house resources," she said.

Stamford Associates head of fiduciary management advisory Carl Hitchman also spoke to delegates on fiduciary management, noting that as pension funds mature, the opportunity to get things right or set things straight will diminish.

Addressing the challenges of how to be able to pay member benefits, Hitchman said to identify how you need to invest to have a realistic expectation of paying member benefits over the lifetime of the scheme. He also suggested schemes map assets to specific cashflows, exploiting the natural characteristics of the assets to mitigate disinvestment risk, and adjusting portfolios to reflect implications of legislation, sponsor covenant risk and risk appetite.

Defined contribution

Changing the focus to defined contribution pensions, NEST senior business development manager Robin Armer, spoke to delegates about the ideal journey a person saving for retirement should embark on, but then compared it to the historical reality. For example, ideally a saver will have saved from their mid-twenties and be actively engaged, whereas in reality most people have never saved and are not engaged.

NEST has applied behavioural insights, and Armer highlighted that young people are loss averse, and generally feel loss at twice as much as they feel gain; he said that this loss aversion drives a persons' behaviour. As a result of this insight, Nest has looked to simplify jargon, and in particular has focused on the names of its own funds. For example, members not wanting the default fund can choose to invest in the NEST Higher Risk Fund, NEST Lower Growth Fund, NEST Ethical Fund, NEST Sharia Fund and NEST Pre-retirement Fund.

"We've labelled the funds very clearly so you know what you are getting into, so if you make the positive decision to move from default to lower growth, it is because you understand that the lower growth also means lower risk, and that's what you want to achieve. We don't call the higher risk fund, a higher growth fund, we call it higher risk."