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Pension Risk Mitigation: reconciling employer and trustee views

Clive Wellsteed
29th April 2009















Reconciling employer and trustee views



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- ◆ The idea of a “road to buyout” is not a new one
- ◆ Employer / trustee perspectives
 - Common destination...
 - ... different journey?

 Current economic climate		
Worst case 30% chance	Central case 60% chance	Best case 10% chance
 <ul style="list-style-type: none"> ◆ Serious deterioration ◆ Bank initiatives fail ◆ Debt and fiscal burden ◆ Echoes of 1990s Japan ◆ Unprecedented insolvencies ◆ PPF burden 	 <ul style="list-style-type: none"> ◆ Economies struggle throughout 2009 ◆ More bank regulation & lending control ◆ Quantitative easing starts to work ◆ Continued deleveraging by banks, households & companies ◆ Deflationary pressure in 2009 & 2010 ◆ Unprecedented gov bond issuance ◆ Reduced corporate profitability / access to funding ◆ Trustees seek improved benefit security 	 <ul style="list-style-type: none"> ◆ Recovery to normal conditions by late 2009

 De-risking options	
De-risking options include:	 Investment strategy
	 Bulk annuities
	 Longevity hedging
Liability limitation / reduction options include:	 Cap pensionable pay
	 Close to future accrual
	 Transfer value exercise



Conversation with Finance Director

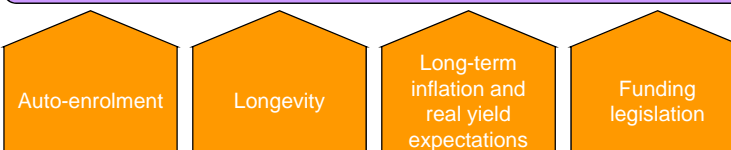
- ◆ How long do you want to still be running a DB scheme?
- ◆ What does “risk” mean to you
 - balance sheet, cash, P&L
 - missing opportunities to reduce risk in the future

... and how much risk do you want to take?
- ◆ Consider non-investment risks
 - mortality, governance, HR
- ◆ Consider alternative risk reduction measures
 - eg risk transfer, longevity bonds
- ◆ Work with Trustees to align objectives and implement strategy



Company pitch to trustees

There is significant upward pressure on defined benefit costs.

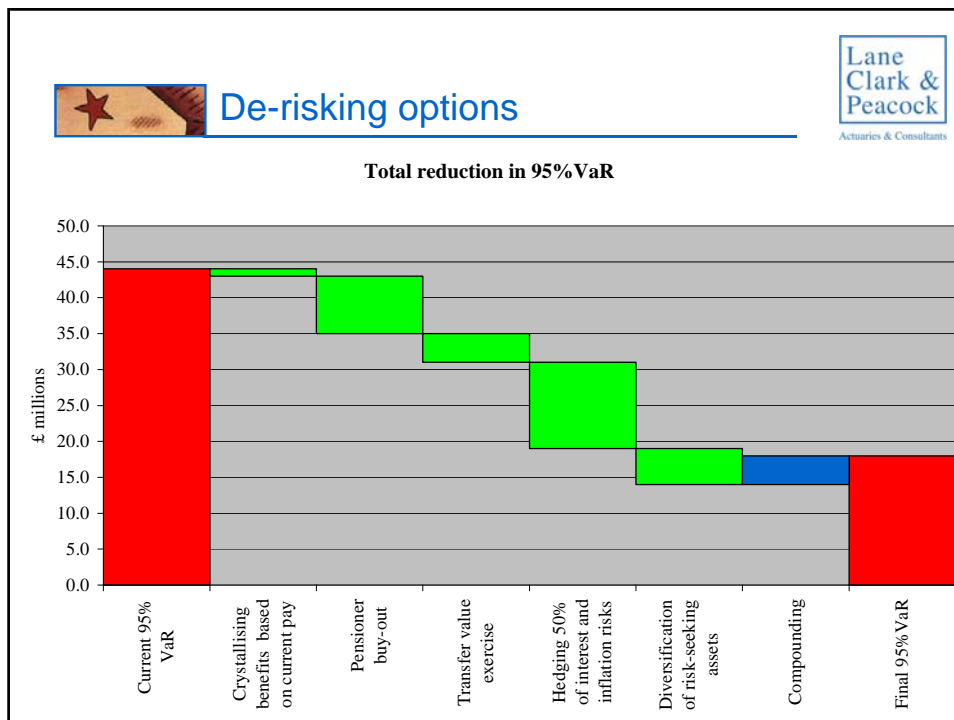


- ◆ “Company view is that funding these additional costs is potentially damaging to the business....
- ◆ and that the market / our competitors are increasingly moving away from defined benefit pension provision
- ◆ the Board and shareholders wish to work with the Trustees to contain / manage down the risks associated with DB provision”

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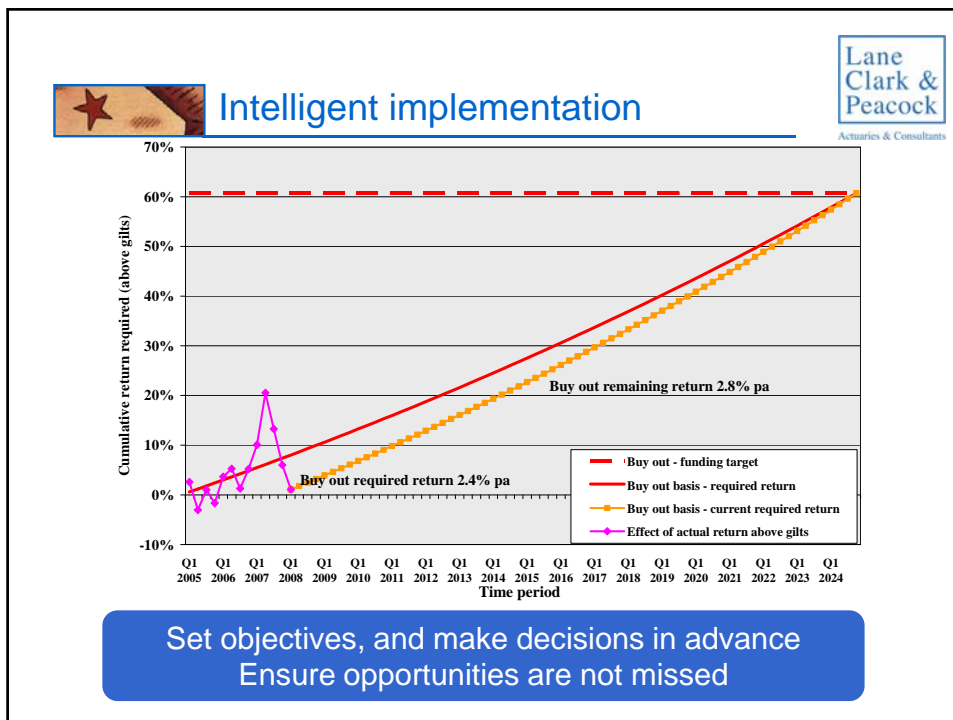
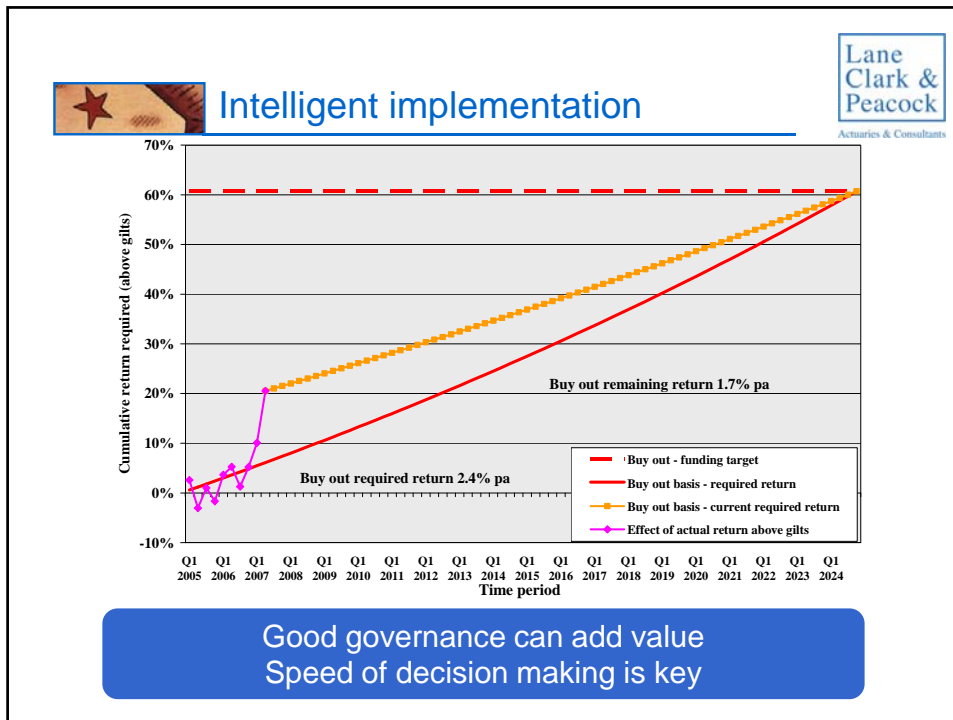
Conversation with Trustees

- ◆ What do you want to achieve? 1
 - consider return, risks, liabilities, employer covenant
- ◆ Don't take unnecessary risks 2
 - hedging interest rates, inflation, currency
- ◆ Don't put all your eggs in one basket 3
 - diversify asset classes, risk factors, manager skill
- ◆ Implement intelligently 4
 - cash flows, switching, timing, value-add opportunities



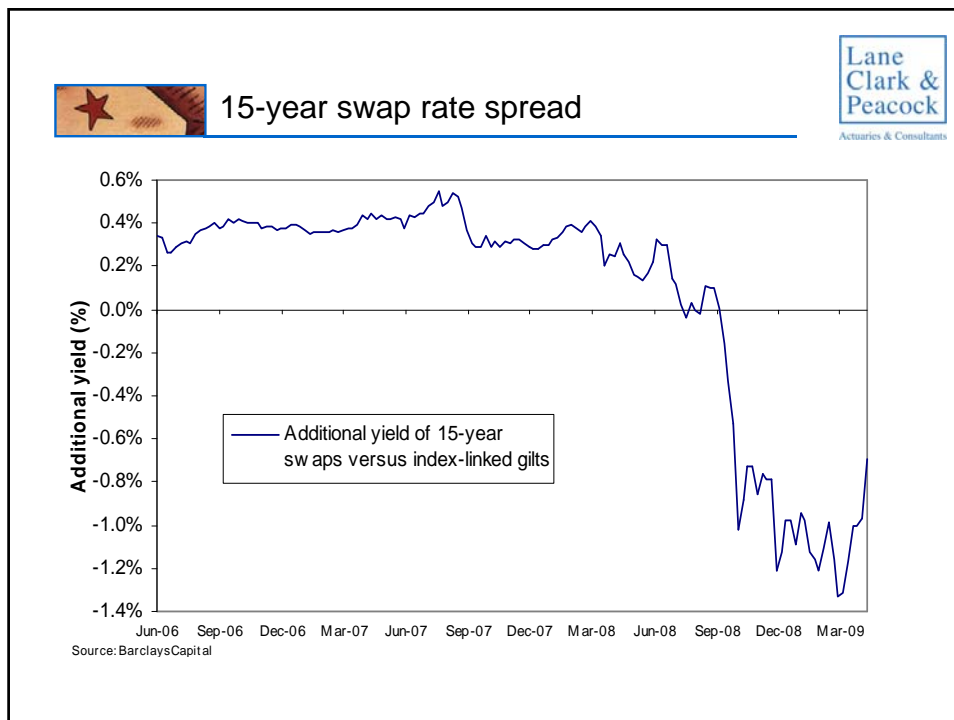
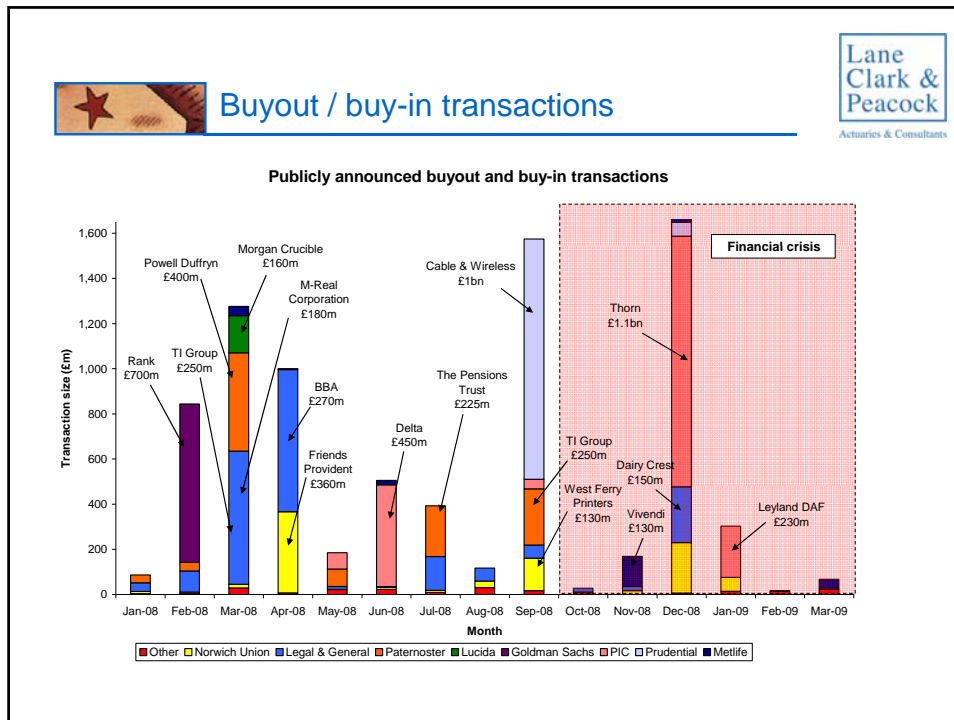


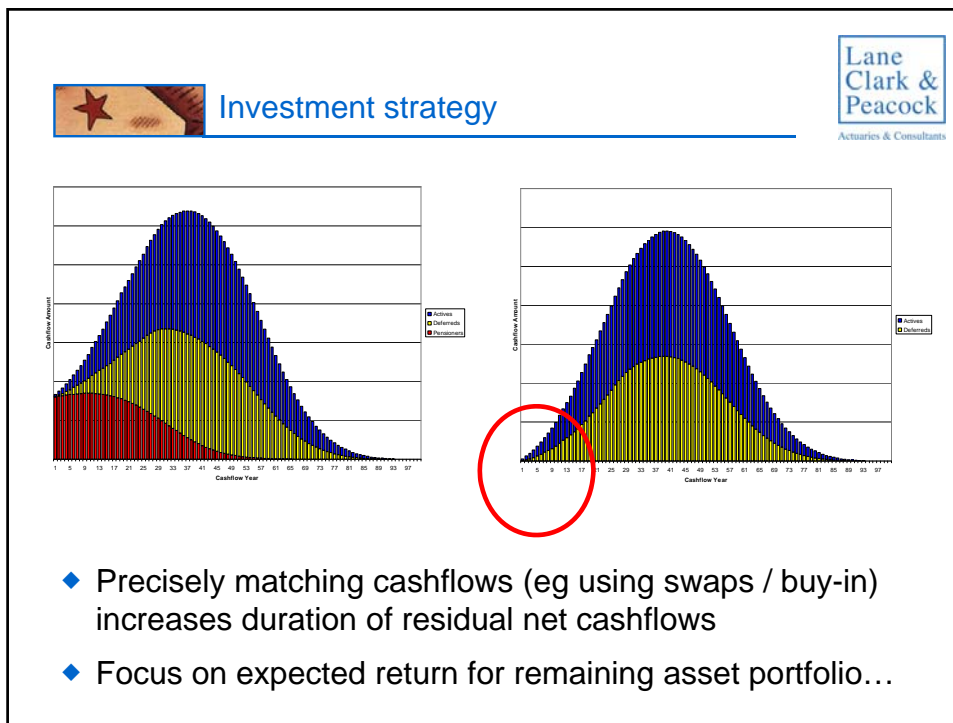
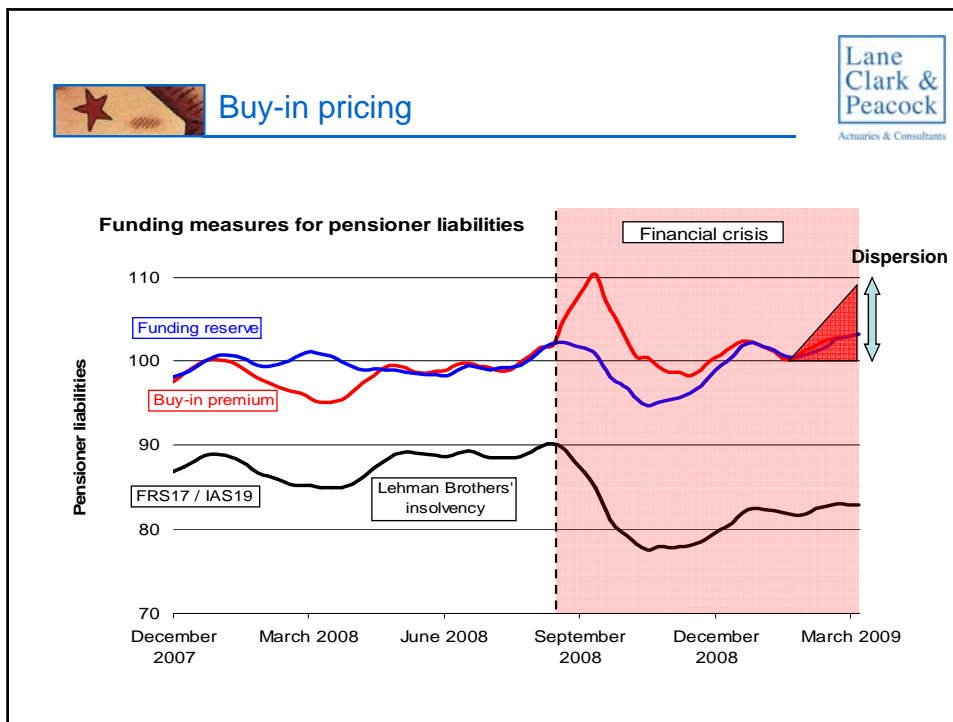
Pension Risk Transfer Seminar





Pension Risk Transfer Seminar







Closing thoughts

De-risking through buy-in / investment strategy / benefit changes can significantly reduce risk

- ◆ Pace of risk reduction is the key discussion point
- ◆ In terms of the next funding valuation:
 - de-risking could support stripping some of the margins for prudence in the discount rate
 - offset to weaker company covenant?

Interests of company and trustee can be aligned



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