



RISK TRANSFER JOURNEY PLANNER

Q1 | 2024

Buy-out and other endgame options

Welcome to Quantum Advisory's Q1 2024 Journey Plan newsletter. Each quarter, our risk transfer team will bring you details of market pricing in relation to various risk transfer options as well as sharing useful tips and experience to ensure that your risk transfer journey is as smooth as possible. This could be as a buy-in (where the members remain in the scheme) or a buy-out (where the members leave the scheme and are paid directly by the insurer).



Pensioner buy-out & buy-in pricing

Overview of insurer pricing

Insurers price business based on gilt and corporate bond yields, plus the cost of setting aside regulatory capital, their desire for new business and how well any particular scheme would fit with their existing portfolio. This means there is no one figure for the buy-out cost for a pension scheme. However, we receive monthly data from a number of insurers which allows us to monitor how pricing moves over time.

Market background – financial drivers

Markets in Q4 2023 were largely stable. Gilt yields in October 2023 reached a slightly higher level than their peak just after the mini-Budget in late 2022, but then fell to end the quarter about 0.75% lower than where they started. Market implied inflation continues to gradually fall, and ended the quarter down about 0.2%. The net impact of these changes will be higher insurer pricing for most benefits.

On the asset side, equities generally ended the quarter at a higher level than where they started, with equity prices up 5-10% and bond prices up 10-15%. The impact on individual schemes will depend on their asset allocation.

IN THIS ISSUE

- Pensioner buy-out & buy-in pricing
- A recent Quantum Advisory buy-in case study



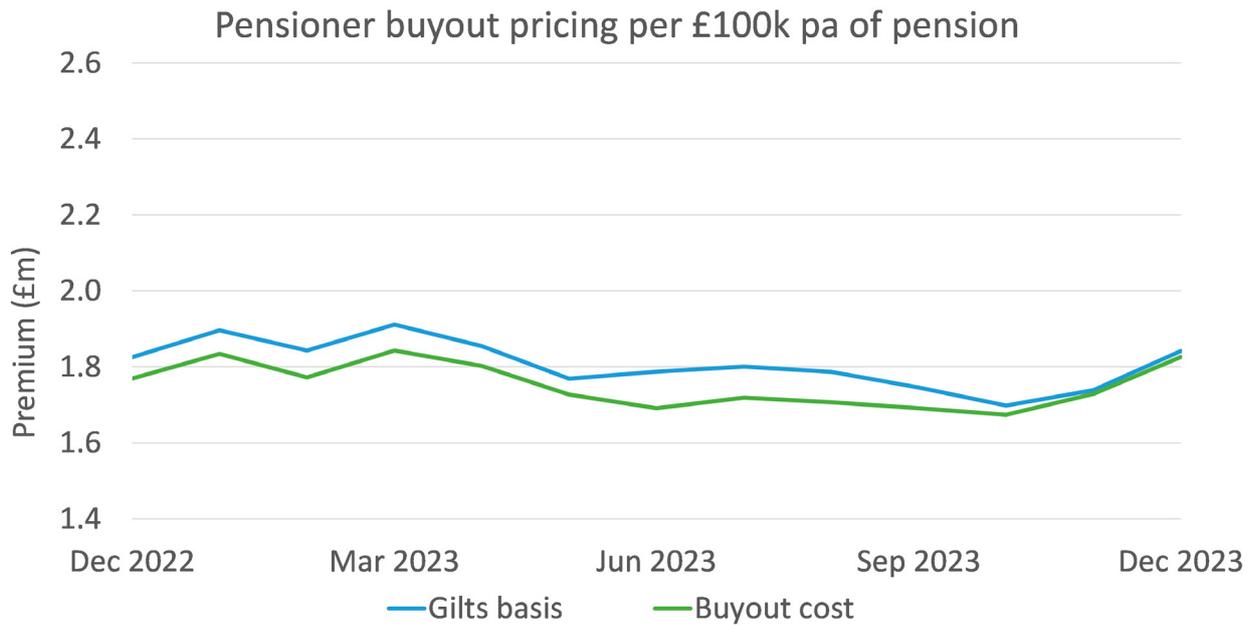
Pricing update and de-risking opportunities

The chart below shows that insurer pricing remains just slightly cheaper than gilts (shown by the green line sitting below the blue line). Buy-ins for pensioners are becoming more expensive but remain available at around 5% less than the cost of funding the same benefits with a portfolio of gilts.

A pension scheme looking to buy bulk annuities as a cash buyer will see this pricing as more attractive than a couple of years ago because prices have come down materially in absolute terms.

The difference between liabilities on a gilts basis and the buy-in/buy-out cost offers an opportunity for schemes with a large proportion of gilts backing their pensioner liabilities to reduce risk for little, if any, cost.

Pricing for deferred members remains higher than for pensioners because of the additional risks they represent for an insurer. A scheme looking to sell gilts to fund a deferred member buy-in would still need to find an additional c10% on top of the value of the gilts.



The buy-in process

Transacting a buy-in will usually take a few months, but there are steps you can take to plan ahead and speed this up. These include:

- Ensuring that all Scheme documentation is in good shape, including common sticking points such as Barber benefit equalisation.
- Ensuring that your membership data is complete and accurate.
- Reconciling GMPs with HMRC (which should be in progress now that HMRC have issued final data).
- Equalising GMPs for differences between male and female benefits (now confirmed to be required by the Lloyds judgement).

Any schemes considering buying bulk annuities should be aware that insurer capacity will ultimately be limited by availability of assets and re-insurance. The steps above will help in showing insurers that you are serious when seeking quotes.

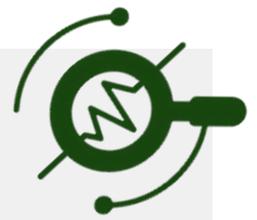
We can assist with planning for a buy-in if you are considering this route. The case study overleaf gives more detail on the steps needed for a buyout and the importance of project planning.

Next steps

Prices vary both between insurers and over time, so a full quote is the only way to obtain accurate pricing. If you would like more information, please speak to your usual Quantum contact.

Disclaimer

Quantum sources information from the insurance market monthly and is reliant on this information to produce pricing updates. This information is high-level and not specific to any individual pension scheme. Pricing for an actual scheme will therefore differ.



Quantum Advisory case study

Quantum Advisory - Enabling the trustees of a £10m defined benefit pension scheme to secure a buy-in through successful teamwork, careful planning and project management

Client : A UK based, not-for-profit organisation

Background

In October 2020, upon the sale of the sponsor's premises, the trustees of a long-standing client of Quantum were provided with a significant lump sum payment into the pension scheme to support ongoing funding. The scheme did not have sufficient funds to complete a buy-out at that stage, but the increase in asset value meant that this became a viable short to medium-term target.

Two years later, the sharp upward swing in gilt yields resulting from the infamous mini-budget in September 2022 filled most of the remaining funding gap. We advised the trustees to become

'buy-out ready' as soon as possible and to look into buying out the scheme's liabilities with an insurer at the first opportunity, which might now be possible without any further sponsor contributions.

After reviewing the risk transfer market, the trustees asked us to lead their buy-out project which included the risk broking aspects. Their objective was to remove the investment, inflation and mortality risks associated with the scheme through a buy-in policy, with the aim of converting this to a buy-out policy and winding up the scheme in the near future.

Detailed project planning was key

We took the lead on agreeing a detailed and achievable project plan with the trustees and sponsor. This was split into three sections, setting out:-

1. The roles and responsibilities of all parties.

This helped us to identify whether there were professional advisers appointed in all areas and whether the current advisers were most suited to guiding the trustees through the buy-in and buy-out exercises. This prompted the trustees to appoint a different legal adviser for the buy-out to the one they used for ongoing work. The sponsor also appointed a legal adviser for any advice they might need.

It was also useful to designate a dedicated buy-out project coordinator at this stage. Quite often, minor delays in individual tasks can impact the overall timescale of the project so regular monitoring of the project plan is an essential part of a transaction being completed on time and within budget.

2. A list of all the key tasks that would be required.

There are many standard tasks that need to be completed for all buy-out exercises, such as carrying out data gap analysis, drafting a benefit specification and obtaining legal advice. However, in this case there were also a number of non-standard tasks, such as removing a deferred revaluation underpin from the benefit structure and reviewing the scheme's AVC policies to ensure they could be discharged easily prior to the scheme wind-up.

3. A timeline of key events.

This section plotted the key tasks on a weekly timeline which clearly showed how long each stage should take and also allowed us to determine when certain mini pieces of work should be carried out optimally. Planning tasks like this allowed individual service providers to be informed in advance of when their work would be required so they could resource effectively, giving more certainty over timescales and budgets.



Quantum Advisory case study:

Enabling the trustees of a £10m pension scheme to secure a buy-in through successful teamwork, careful planning and project management



Approaching the Market

We spent the initial few months ensuring that the scheme's membership data and documentation were in good order, after which we were in a great position to approach the market for indicative quotations.

After receiving quotes from three insurers, we found one in particular who was very approachable and keen to help the client by providing them with an idea of live pricing on an indicative basis, in a reasonably short timeframe. The insurer was attentive and sympathetic to the trustees' cause, and offered a deal at an attractive price despite this being the busiest time for the UK buy-out market. Due to the unprecedented level of activity in the market, we made a call that the most likely way to achieve a full scheme buy-in quickly, before the Christmas period, was to negotiate terms with the insurer directly and to make them aware of the scheme and sponsor's specific circumstances. The trustees transacted with the insurer in October 2023, leaving the scheme with a small surplus and no requirement for further funds from the

sponsor.

Conclusion

Taking the same tried and tested approach of successful teamwork, careful planning and project management, we are now working closely with the trustees through the next phase of the project. The 'data cleansing' stage presents the scheme's data in an insurer-friendly format so it can be transferred to the insurer seamlessly for them to carry out the ongoing administration tasks. Once this is complete, in around 12 months' time, we will complete the buy-out with them and wind up the scheme. The sponsor can then concentrate on their commercial operations, supporting businesses in their local area.

The trustees and the sponsor were delighted to complete the buy-in process quicker and cheaper than originally anticipated and all parties were comforted knowing that the vast majority of pension risks have been mitigated. We were delighted to successfully deliver the joint objective of the trustees and the sponsor as planned.

Adam Cottrell, Lead transaction advisor at Quantum Advisory, said:

"Having worked diligently with the Trustee and client since 2010, it was very fulfilling to see them achieve their long-term strategic objective as planned and provide additional security for Fund members.

"One of the main challenges was to complete the transaction so seamlessly at an extremely busy time for the market. Knowing how this enhanced level of pension security will benefit members over the long term, at a time when everyone's finances are so stretched, makes this a particularly rewarding end to a successful project. The Trustees and the Client put their trust in us to make the right moves, at speed, at key milestones of the transaction, something which is so often critical in getting this size of deal over the line. We are very proud to have helped them reach this key milestone on their journey to buy-out."

This quarter's newsletter was prepared by Simon Hubbard. Simon sits on the risk transfer team at Quantum Advisory, helping to manage projects and working with major insurers to track market prices and market sentiment. He is also a member of Quantum's Defined Benefit Strategy Group and assists with the development of Quantum's in-house actuarial models.

Simon holds a Scheme Actuary certificate and is currently Scheme Actuary to a number of pension schemes. He has fifteen years of experience delivering trustee and corporate consulting advice including valuation negotiations, benefit change projects, company pensions accounting and member option exercises.

Simon is also an Examiner for the Institute and Faculty of Actuaries, helping to develop the course content and set the exam in financial economics.



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Who we are

Established in 2000, Quantum Advisory is an independent financial services consultancy that provides solution based pensions and employee benefit services to employers, scheme trustees and members.

We design, maintain and review pension schemes and related employee benefits so that they operate efficiently and effectively and are valued by employees. This means that you can get on with doing the things that you do best, therefore saving you time and money.

Products and services

We offer a range of services to companies and pension trustees, all designed to focus on your specific needs, including:

- Actuarial services
- Administration of defined contribution and defined benefit pension schemes
- Banking, accounting and pensioner payroll
- Company advice
- Employee benefits consultancy
- Governance
- Investment consultancy
- Pension and employee benefit communications
- Risk benefits advice
- Pension scheme wind up
- Trustee training
- Flexible benefits

Risk transfer team

We have offices in Amersham, Birmingham, Cardiff and London. Give us a call to see how we can help with your risk transfer, pension and employee benefit challenges.

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