

While economic turmoil has caused a slowdown in bulk annuity transactions, Prudential's Andy Reed assesses how schemes can prepare themselves now to be ahead of the game when financial markets improve

The waiting game

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There is a danger lurking for schemes waiting to de-risk 'when the timing's right': market capacity. With all eyes on the economy and pension deficits it may have gone unnoticed that a few providers took a strategic step back from the defined benefit risk management market to focus on their 'core markets'. As a result, market capacity could become a real concern for schemes looking to de-risk their pension liabilities. When the economy does stabilise, there is likely to be a stampede as schemes vie to quickly reduce exposure - but only those schemes in the best shape to transact are likely to see their wishes being met.

The winners and losers will not only be determined by those best placed to afford solutions, but also by those who have already made the necessary preparations. It will be all too easy to become totally embroiled in fixing the scheme funding situation and then breathe a huge sigh of relief when things finally look better. But the opportunity to de-risk may have gone! So how CAN schemes prepare themselves now?

Agree key aims

Firstly, it's vital that trustees and sponsors agree on their key aims for the scheme. Regardless of the funding position, both parties need to be fully aligned to one strategy to ensure the most appropriate solutions are implemented effectively. For example, do you have a long term strategy of gradual de-risking, or is there a desire to take significant steps that provide an immediate impact? Of course, both parties should seek independent advice throughout the process, involving employee benefit consultants, scheme actuaries and lawyers. But collaboration is paramount.

Data cleansing

Data cleansing sounds like one of those horrible jobs to leave for tomorrow, but it is a vital part of risk transfer. Starting data cleansing early will save you both time and money. The more accurate your data, the more accurate the quotes you receive will be – and the smaller the risk of any nasty surprises when you actually transact. In fact, with accurate data you may need fewer quotes to get



to the point of transacting, which will cost you less. In some cases, providers have refused business due to the risks involved in poor quality data - regardless of the scheme's ability to pay for solutions. Starting data cleansing exercises early will help avoid disappointment and unnecessary costs further down the line.

Assess the solutions

There is no single right or wrong way to de-risk, so professional guidance from corporate advisers will be essential to help you select the most effective solutions for your scheme. De-risking solutions can range from simply hedging investments through to full buyout as part of a scheme wind-up, although most schemes will be looking to implement solutions somewhere in between (with buyout as a possible 'end-game'). There are various options available and schemes can combine these over time to develop a more affordable and manageable de-risking route-map. Take time now to understand what is on offer.

Provider selection

Having agreed on the best approach, there is the equally fundamental question of who to place your business with – another key decision requiring input from corporate advisers. Trustees should already be thinking about the type of credentials and strengths that will be

important to them, so they can engage with the right providers. Pension provision is a long-term commitment. The livelihood of scheme members is at stake – and with it the reputations of trustees and sponsors! Choosing the right provider with the ability to fulfill that promise for the full duration is essential. Trustees need to think about what they are buying, how long they are buying it for and who they are buying it from.

Investment strategies

Being already invested in assets that insurers are happy to accept (via in-specie transfer) could prevent a huge headache. Trying to conduct large scale disinvestments (sometimes at a time when the investment market may be unwilling to trade into the assets being sold) can prove extremely difficult. Therefore, matching investment portfolios to suit the desired de-risking solutions will be beneficial. Providers and advisers can help schemes identify this in the lead up to de-risking.

Ultimately, the trick will be avoiding the trap of the waiting game. Those who simply wait for better times may find themselves sitting on the sidelines while others de-risk.



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