The YMCA Pension and Assurance Plan

Annual Actuarial Update as at 1 May 2013

professional | proportionate

Contents

1. Introduction

Purpose of this Report

1.1 This report, addressed to the Trustee, provides an update of the funding position of The YMCA Pension and Assurance Plan (the ‘Plan’) as at 1 May 2013 for the purposes of Section 224 of the Pensions Act 2004.

1.2 That Act introduced a new Statutory Funding Objective requiring defined-benefit pension schemes to have sufficient assets to cover their ‘technical provisions’, namely the amount needed on an actuarial calculation to make provision for the accrued benefit liabilities as part of a planning (budgeting) exercise.

1.3 To assess whether the Plan meets the Statutory Funding Objective, full actuarial valuations have to be carried out at least every three years. Where such a valuation indicates a funding deficit, a Recovery Plan is required setting out the steps to be taken to meet the Statutory Funding Objective and the period within which it is to be achieved. The latest such valuation of the Plan was carried out as at 1 May 2011 and is documented in my report dated 22 March 2012. The next full valuation is due to be carried out not later than as at 1 May 2014.

1.4 In the meantime, the Trustee must obtain annual updating reports on developments affecting the Plan’s technical provisions and assets since the last actuarial valuation was prepared. This report is the second such update. The previous update was carried out as at 1 May 2012.

1.5 This report enables the Trustee to review its funding documents and consider obtaining a full actuarial valuation for an intervening year if it seems that events have made it unsafe to continue to rely on the results of the previous valuation as the basis for the current level of contributions.

1.6 This report and associated work complies with the Financial Reporting Council’s Technical Actuarial Standard R: Reporting Actuarial Information, Technical Actuarial Standard D: Data, Technical Actuarial Standard M: Modelling and with the Pensions Technical Actuarial Standard.

> This report is solely for the purpose indicated above. It should not be relied upon for any other purpose and it should be noted that neither I nor Xafinity Consulting Limited accept liability to any third party in respect of the contents.
>
> The Trustee must ensure this report is made available to the Participating Employers within seven days of receipt.

2. Methodology and Assumptions

Methodology

2.1 The actuarial method used for this update is the Projected Unit Method. This is the same actuarial method as was used for the actuarial valuation as at 1 May 2011. Further details are available in my report to the Trustee on that valuation, dated 22 March 2012.

Financial Assumptions

2.2 As part of the actuarial valuation as at 1 May 2011, the Trustee prepared a Statement of Funding Principles the contents of which were agreed with the nominated representative of the sponsoring employers. In carrying out this update, I have set the financial assumptions using the same principles as in that Statement but with allowance for changes in financial markets in the interim. This is not to say that if a formal actuarial valuation had been conducted at 1 May 2013, the assumptions would be those set out below. A formal valuation would involve a new discussion about the appropriate ‘strength’ of the assumptions.

Financial Conditions

2.3 The following table sets out the principal changes in financial markets since the previous actuarial valuation and annual update, as they relate to setting the financial assumptions:

	Annual Update as at 1 May 2013	Annual Update as at 1 May 2012	Actuarial Valuation as at 1 May 2011
Annualised 20 year fixed interest government bond yield	2.64%	3.06%	4.18%
Implied market price inflation	3.10%	3.00%	3.60%

2.4 The market factors show that underlying bond yields have decreased by around 1.5% since the 2011 valuation, with the implied long term rate of annual retail price inflation having decreased by around 0.5%.

2. Methodology and Assumptions

2.5 Factoring these changes into the agreed principles, I have carried out this update using the following financial assumptions:

	Annual Update as at 1 May 2013	Annual Update as at 1 May 2012	Actuarial Valuation as at 1 May 2011
Discount Interest Rate			
- **before Retirement**	4.65%	5.10%	6.20%
- **after Retirement**	3.40%	3.85%	4.95%
Retail Price Inflation	2.90%	2.80%	3.40%
Consumer Price Inflation	2.40%	2.30%	2.90%
Pension Increases			
- **RPI max 5%**	2.90%	2.80%	3.40%
- **RPI min 3% max 5%**	3.40%	3.30%	3.60%
Deferred Pension Revaluation	2.40%	2.30%	2.90%

Demographic Assumptions

2.6 I have used the same demographic assumptions for this update as adopted for the actuarial valuation as at 1 May 2011, being those set out in the Plan's Statement of Funding Principles dated 24 March 2012.

2.7 Following my briefing paper on cash commutation factors dated 27 September 2012, it was decided at the factor review that the commutation factor would be increased to 12.20 at age 65. This increase was implemented to reflect the increase in life expectancy and lower investment returns following the actuarial valuation as at 1 May 2011.

2. Methodology and Assumptions

2.8 These are summarised in the following table:

Mortality before Retirement	PNMA00/PNFA00 with medium cohort improvements (minimum improvement of 1% per annum)
Mortality in Retirement	PNMA00/PNFA00 with medium cohort improvements (minimum improvement of 1% per annum)
Cash commutation	75% of members are assumed to commute 25% of their pension for cash. The assumed future conversion rates are based on the factors agreed following the factor review on 27 September 2012.
Retirements	Allowance for early retirement between the ages of 60 - 65 with adjustment for early retirement factor as appropriate. Valued at earliest age at which entitled to all of part of the pension unreduced. Some pension reduced by Plan early retirement factors where appropriate.
Marital statistics	80% of male members and 70% of female members are married with wives 3 years younger than their husbands.

3. Data

Membership Data

3.1 The principal source of data on the Plan membership is the actuarial valuation as at 1 May 2011. For example, that valuation recorded each member against their status at the time.

Changes to Membership

3.2 This update requires me to comment on how I have taken membership changes into account. I have allowed for membership changes by adjusting the membership data for all known member movements between 1 May 2011 and 1 May 2013. The updated member statuses were then used for the current annual update. This updated membership data was supplied to me by our administration department and is summarised in Appendix A. Having reviewed this data I believe that its quality and completeness are adequate for the purpose of the valuation.

Assets

3.3 I have been supplied with a provisional value of the Plan investments as at 1 May 2013 of £77,113,792; I have also taken account of estimated net current assets of £270,217.

3.4 In addition, there are a number of insured annuity contracts which I have valued on a consistent basis to the corresponding pension liabilities. They have a value of £7.7m.

4. Results

Past Service Position

4.1 I have compared the assets held at 1 May 2013 with the value of the benefits earned by members. The following table shows the results of this calculation together with the comparative figures from the previous annual update and valuation:

	Annual Update as at 1 May 2013	Annual Update as at 1 May 2012	Actuarial Valuation as at 1 May 2011
Technical Provisions (ie liabilities)	141.7	125.6	103.3
Assets	85.1	75.2	71.0
Deficit	(56.6)	(50.4)	(32.3)
Funding Level	60%	60%	69%

4.2 The table shows that the deficit of £50.4m as at 1 May 2012 has increased to an estimated deficit of £56.6m as at 1 May 2013. The main reason for this deterioration is the change in market conditions (in particular a decrease in the gilt yield) leading to revised assumptions which place a higher value on the liabilities.

4.3 The following table summarises the financial effects of the above and other factors which have influenced the changing financial position.

	£m
Surplus/(deficit) as at 1 May 2012	(50.4)
Interest on deficit	(1.6)
Investment return higher than assumed	5.3
Impact of change to cash commutation factors	(2.4)
Change of basis	(12.0)
Deficit reduction contributions	3.0
Member movements	1.2
Other	0.3
Surplus/(deficit) as at 1 May 2013	(56.6)

xafinity

5. Further Considerations

Investment Strategy

5.1 Some of the Plan's liabilities are linked to inflation via either pension increases in payment or revaluation in deferment. The assets that would most closely match the liabilities are a combination of index-linked gilts to match these inflation-linked liabilities and fixed-interest gilts to match the fixed liabilities of the Plan.

5.2 It is a result of the mismatch between the actual assets held by the Plan and these notional "matching assets" that there is likely to be volatility in the past service funding position. The Plan investments are mismatched because the Trustee has invested some of the Plan's funds in risk-bearing assets such as equities that are expected to produce higher future returns than gilts and other bonds. The risk that must be traded off against these expected higher returns is the increased volatility of the Plan's returns and the higher risk of default.

5.3 The Trustee has chosen the current investment strategy in the light of their understanding of the strength of the Employers' covenant. It is not an inappropriate strategy but the Trustee should recognise the volatility that it inevitably implies.

5.4 The basis chosen by the Trustee to value the Plan's liabilities recognises the investment strategy as described above by building in an allowance for a proportion of the Plan assets to achieve returns in excess of the yields available on gilts at the valuation date.

5.5 It is important that the Trustee continues to review their investment strategy as the Plan matures. The strategy should be reconsidered in the event of any weakening in the Employers' covenant.

5.6 If equities perform strongly in the future the funding position of the Plan would improve, assuming that bond yields are stable. In contrast, poor future equity returns would lead to a deterioration of the Plan's funding position if bond yields remain stable. Similarly, if equity returns are stable but bond yields change, the funding position would vary.

5.7 If the Trustee wished to reduce the risk of such volatility they would need to match the assets to the liabilities to a greater degree by investing more in Government stocks or other bonds. By following such a strategy, a fall in bond yields (and the associated rise in liability values) would be offset by a rise in the value of the Plan's assets. However, bonds and, in particular, Government stocks are a lower risk asset class and consequently the long term expected returns on bonds and gilts are lower than the expected future returns on more risky assets such as equities.

5. Further Considerations

Employer Covenant

5.8 I have not allowed for any change in the Employers' covenant (i.e. the risk that the Employers could prove unable to continue future contributions or that the Plan will not recover the deficit upon insolvency). The Trustee should review the current strength of the covenant regularly.

5.9 If the Trustee feels that the covenant has weakened then it may be appropriate to review the Recovery Plan and Schedule of Contributions. I have assumed here that the covenant has not declined since the last valuation as at 1 May 2011.

Buyout Cost

5.10 I have not reported the buyout position as at 1 May 2013 in this report, but we will be preparing such calculations for the Trustee and providing them separately.

6. Summary

Implications for the Recovery Plan

6.1 Following the funding deficit revealed by the actuarial valuation as at 1 May 2011, the Trustee established a formal Recovery Plan. This requires additional employer contributions of £2.97m per annum, payable in equal monthly instalments for a period of 11 years commencing from 1 May 2012 and increasing by 3% at each 1 May thereafter. Based on conditions as at 1 May 2011, these payments were estimated to be sufficient to clear the funding shortfall by 1 May 2023.

6.2 This report identifies deterioration in the existing funding position of the Plan. This will have a negative influence on the length of the recovery period if there are no changes made to the contributions being paid to the Plan.

6.3 Based on conditions as at 1 May 2013, I estimate that payments in accordance with the Plan's current Schedule of Contributions would be expected to clear the funding shortfall by the end of 2026.

6.4 The Recovery Plan will be due for formal review as part of the next full actuarial valuation of the Plan, which is to have an effective date no later than 1 May 2014.

6.5 The Trustee should note that there is likely to be volatility in the past service funding position as a result of the mismatch between the actual assets held by the Plan and the notional "matching assets".

6.6 Since the current annual update as at 1 May 2013 there have been some changes in the market conditions. The long dated gilt yields have improved therefore there is likely to be a decrease in the Plan liabilities.

Signature:		**Date:**	
Name:	Colin Stewart Price	**Qualification:**	Fellow of the Institute and Faculty of Actuaries
Address:	Xafinity House 42 - 62 Greyfriars Road Reading Berks RG1 1NN	**Name of Employer:**	Xafinity Consulting Limited

Appendix A - Membership Data

This Appendix summarises the membership data used for the current annual update, as well as showing comparative figures from the previous valuation as at 1 May 2011.

Plan membership data, as at the annual update, was supplied to me by Xafinity Consulting administration team who have been appointed as administrators to the Plan by the Trustee. I have relied on the accuracy of the information, having taken reasonable steps to satisfy myself as to its adequacy for the purposes of my calculations.

A summary of the membership data is set out below.

Deferred Pensioners

	Annual Update as at 1 May 2013 £m		Actuarial Valuation as at 1 May 2011 £m	
	Number	Deferred Pension (£m)	Number	Deferred Pension (£m)
Males	492	1.802	552	2.031
Females	604	1.088	652	1.237
Total	**1,096**	**2.890**	**1,204**	**3.268**

The deferred pension amounts in the above table are as at the respective dates of leaving.

Current Pensioners

The following table shows the number of pensioner members and includes both plan pensioner members and insured pensioner members. However, the annual pension shown is only that of the pensions currently in payment from the plan.

	Annual Update as at 1 May 2013 £m		Actuarial Valuation as at 1 May 2011 £m	
	Number	Annual Pensions (£m)	Number	Annual Pensions (£m)
Males	271	1.322	248	1.097
Females	277	0.596	253	0.435
Total	**548**	**1.918**	**501**	**1.532**