Pensions Management Institute

ACHIEVING PENSIONS EXCELLENCE

COVID-19

Your Industry Guide

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Letter from the CEO

The coronavirus crisis has emerged as the worst peacetime emergency of the modern era. Its impact has been both immediate and wide-ranging and has disrupted all aspects of everyday society. Within the specific context of the pensions industry, its influence has been colossal. The devastating impact on the international markets has resulted in massive reductions of asset values and has seen trustees and sponsors struggle to address funding issues. As many as eight million employees may have been placed on the Government's emergency furlough scheme, and as a result, many are struggling to balance the competing priorities of debt management and continued pension scheme membership.

Lockdown has seen trustees having to manage new challenges to maintain appropriate governance standards, such as dealing with the consequences of illness among their own board members, how to conduct regular board meetings and maintain effective communications with their advisers and scheme members.

Taking these factors into account, trustee boards have been forced into making radical decisions in order to be able to continue functioning. There has been a dramatic and immediate shift to accommodate the challenges – and opportunities – of holding virtual meetings. There has been a grim but necessary requirement for them to review risk registers in order to address critical issues that did even exist as recently as six months ago. Another unfortunate development has been a growth in pension scams, as desperate members seek solutions for short-term cash shortages.

However, it has become clear that the industry has responded to the emergency with pragmatism, creativity and professionalism. To date, those working within the pensions sector have shown a commendable capacity to adapt and innovate in response to new challenges. It is entirely likely that many changes adopted over the last month will prove to be permanent as rapidly-improvised solutions prove to be superior to long-established procedures. With this in mind, now is a golden opportunity for pensions professionals to exchange ideas to ensure that we are not only prepared to cope with the immediate emergency, but can look forward to working more effectively in future. Whilst COVID-19 has had a terrible impact on society, one we will never forget, we should be proud of our capacity for resilience. A terrible situation has brought out the best in us.

Gareth Tancred
Chief Executive

What does the pandemic mean for long-term investors?

Craig Mackenzie, Head of Strategic Asset Allocation, Global Strategy, Aberdeen Standard Investments

The COVID-19 pandemic has had – and is still having – a terrible human cost. Many are facing fears for their lives and livelihoods, and for those of their families and friends. At such a time, looking at your investment strategy seems trivial. But once we've each dealt with the outbreak's most pressing concerns, we do need to think about how it will change the shape of our investments in the future.

Around the world, share prices are in bear-market territory. This means they have dropped more than 20% from an earlier high point. But in every bear market, there comes a time when shares and other so-called 'risk assets' start to look very cheap. This is the point at which brave long-term investors start to buy them again. When this happens, markets find their bottom and investors can be rewarded as prices rise once again.

Knowing when and how to buy comes with difficulties, though. How can we be sure that share prices have tumbled all the way to the bottom? Is there a way to help us make the decision?

Strategic asset allocation

Strategic asset allocation (SAA) is about giving us a structured framework to help make these difficult choices. When times are good, investors are relaxed and risk assets are expensive, SAA tells us to reduce exposure to risk. When the opposite is true, SAA says we should take on more risk.

Our estimates of long-term returns for various asset classes drive the SAA process. The table below shows our provisional estimates for UK and US equities and government bonds. Since markets are so volatile, we have taken an unusual step, predicting outcomes based on several different possible starting price levels. It is likely that we will revise our forecasts several times this year as things become clearer.

Selected asset classes 10 year total return at various starting price levels, local currency % pa

	US Equities (S&P 500)		UK Equities (FTSE100)	
	Starting Index Level	**10Y TR**	**Starting Index Level**	**10Y TR**
Pre-crisis forecast (end Jan 2020)	3380	4.1	7409	8.0
Level 1 30% lower	2400	7.1	5050	11.0
Level 2 45% lower	1800	9.3	3950	12.6
Level 3 55% lower	1500	10.6	3300	13.7
	US Treasuries		**UK Gilts**	
	10Y Yield	**10Y TR**	**10Y Yield**	**10Y TR**
Pre-crisis forecast	159	1.3	63	0.4
Level 1	60	0.6	15	-0.1
Level 2	-20	0.5	-20	-0.5
Level 3	-20	0.5	-20	-0.5

**Once government bond yields hit zero, they can't fall much further. That's why levels 2 and 3 are the same.*

The table shows estimates for annualised expected returns (in percentage terms) at equity prices roughly 30%, 45% and 55% lower than end-January 2020. The index levels represent the performance of a basket of large market-capitalisation equity securities and the relevant ICE Bank of America sovereign bond indices (comprising bonds of various maturities). We have selected the 10-year maturity government bond yield levels (in basis points) to roughly match. Forecasts are not a reliable indicator of future results and there can be no guarantee that these will be achieved.

At the moment, equities outside the US look cheap compared to the past. For US shares, the value for money is less obvious.

In our pre-COVID-19 forecast, the gap between equities and government bonds was quite small, suggesting a fairly modest reward for taking equity risk. At that point, our SAA suggested a cautious portfolio with less exposure to equities and more to emerging market sovereign bonds and US corporate bonds. Now, the gap is very large, so adding more weight to equities is more worthwhile for long-term investors. But this decision is not an easy one. We must be able to answer some important questions before we make the move.

How bad will the economic damage be?

Two factors will determine the extent of the damage from the coronavirus crisis:

- The duration of the lockdowns that governments have put in place
- How well fiscal and monetary policy act to counter the economic damage they are doing

Lockdowns are having immediate, and severe, effects on economies. We don't yet know how long they will last. While events in China and South Korea offer some hope, it is uncertain whether the measures taken by Western countries will be as effective.

On the other hand, the extraordinary measures governments and central banks are taking should help to reduce the economic cost. These include large injections of cash to support incomes and moves to slash interest rates. While these actions are certainly helping materially, they will not be able to stop large-scale business failures and job losses.

As a result, our economists' latest forecast is for global gross domestic product (GDP) to shrink by 8% in 2020. This is much worse than what happened in the global financial crisis (GFC). On the other hand, they think it is likely that we will see a very large rebound in GDP. They expect this to start towards the end of this year, eventually making up for most, but not all, of the losses. Of course there are huge uncertainties in this forecast, in both directions.

In the equity market forecasts shown in the table, we have assumed that the permanent loss of capital will be at a similar level to that caused by the GFC. But even with these fairly severe assumptions, the long-term rebound more than offsets the initial damage to share values.

What if the recession were to turn into a deep and lengthy slump? In that case, gains for investors would be smaller and the point at which they should buy equities would move further into the future. But investors receive a reward in return for taking on the higher risk (compared to owning government bonds) of holding equities. This 'risk premia' should still be attractive.

How would a regime shift affect investors?

Three things have remained very low since the GFC: interest rates, demand levels and inflation. But the shock caused by the global pandemic together with the fiscal and monetary policy response may be so profound that it changes the investment 'regime'.

A shift could go one of two ways. On one hand, long lockdowns and weak policy responses could cause demand to fall further, leading to a deflationary slump. In such an environment, government bonds become more appealing. Low growth means that equities do poorly, but with deflation, government bonds become more valuable in real terms.

On the other hand, unprecedented fiscal policy could combine with massive central bank action to push inflation much higher. Such an environment tends to be positive for equities which can keep pace with inflation, but fixed income assets would lose value in real terms. After 50 years of mixing equities with government bonds in their portfolios, investors would need to look for alternative ways to diversify their holdings.

On balance, we think that once this crisis is over, we will most likely return to the current situation of low interest rates and low inflation. The caveat is that the risk of either of the outcomes noted above – deflation or high inflation – is now much higher. We'll know more as the crisis progresses, but it's likely that a nimble approach to SAA will be needed.

What about timing?

As shown in our table above, the opportunity for investors is large, and is largest for non-US equities. A recovery from the current recession, propelled by unprecedented amounts of stimulus, could well result in annual equity returns of 20-30% over the first two years.

The sensible approach for a long-term investor is to gradually shift their risk profile from cautious to risk-taking. A gradual shift means they can 'average' back into the equity market. This reduces the risk of buying too soon or too late.

A good point of entry may be when numbers of Covid intensive care cases stop rising in the US. It won't be the end of the crisis, but the tide will have started to turn. We'll also have a better sense of the economic damage done, the scope for ongoing containment and the speed of recovery.

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Investors should be aware that past performance is not a guide to future results. The value of investments, and the income from them, can go down and you may get back less than the amount invested.

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Craig Mackenzie, *Head of Strategic Asset Allocation, Global Strategy*

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We provide expertise across a breadth of markets, asset classes and investment approaches. Approximately 1,000 dedicated investment professionals are located globally, close to our clients and the markets where we invest. Additionally, 500 client specialists work closely with investors and advisors to understand our clients' needs and deliver world class investment solutions.

Pension administration: locked down but open for business

Julie Walker APMI DIEB, Principal and Senior Pensions Manager, Barnett Waddingham

The midst of a pandemic isn't the place for platitudes or easy assurances. With clients, colleagues and competitors all travelling down the same relentlessly bumpy road, any talk of 'seamless homeworking switchovers' massively understates the journey that brought us from early March to here.

- Pension administration operates in a joined up world and we can only control a small part of it. Information and monies flow through our hands, connecting to a complex network of corporate, financial and communication systems. Banking, HMRC, postal, insurance, investment, property and a myriad of sub-processor services are all part of our overall process flow. There's a very finely balanced domino effect in play here - if one part falls, every other part is at risk.

- Our people are operating in a joined up world where the lines have necessarily blurred. None of us expected to combine work with childcare, home-schooling, elderly relatives, financial pressures, loneliness, social distancing, frustrated teens and competition for broadband access in crowded homes full of worried but working people. None of this is the carefully crafted homeworking solution envisaged in our people policies.

BCPs aren't really built for such far-reaching and transformational challenges. Yet, collectively, TPAs and our counterparties are making it work. The dust is being knocked off outmoded or inefficient processes and we're finding better ways for our interconnected industries to work together. The frantic 'made-do, mend, extend, reinforce and prioritise' responses that got us all through the first few weeks are laying down new foundations for the future.

Lockdown - what's the worst that could happen?

Phase 1 of working under Covid-19 conditions (the 'where we work' question), was about logistics. Phase 2 ('how we work'), is about how we adapt when the old ways just aren't an option any more.

The hard facts are we don't know how long lockdown and social distancing are going to last and we don't know if this is a one-off or will come back around again in a few months' time. The national psyche may only be primed to cope with lockdown extensions in manageable three week chunks, but we need to be thinking in terms of three, six, nine months and beyond. The best case scenario would see the world somehow back to normal and staying that way by summer. However, in an unfolding crisis, you don't plan for the best case, you plan for the worst, look right down the line at all your key dependencies, anticipate some or all of them failing, and then adapt as much as you can to that new reality.

This is the thinking we're seeing behind major Phase 2 developments, with many providers massively accelerating member online access rollouts, secure document exchange facilities, automated ID verification, remote printing solutions, and electronic approval processes. At Barnett Waddingham we were fortunate that much of the necessary IT infrastructure, services and contractual agreements were already in place, but we're hearing the same story across the industry as the major TPAs push to compress the development work of months and years into days and weeks to keep the admin wheels turning

Case study – member approaching retirement

Pension administration processes are often multistage, with many moving parts. The simplified example shows how, over the course of just a few weeks, quick technological solutions have been substituted for long established processes, helping to mitigate some or all of the process risk in each stage as we work with the realities of Covid-19.

February 2020	Risks	May 2020
Hard copy retirement options are prepared and printed by the administrator, for issue to the member's home address.	Office closures and IT security mean remote working teams do not have access to printers to issue hard copy option pack.	Basic member online access made available to all scheme members on a 'no frills' basis, providing immediate access to all member specific communications at the approval stage. Where hardcopy is required, third party printing contracts and testing implemented, integrating external printing with the existing production process to maintain appropriate internal controls.
Completed option paperwork and original birth certificate/ passport mailed by member.	Social distancing - members unable or unwilling to visit post offices to securely mail original documents/option forms.	Secure document exchange made available so that members can upload copies of their paperwork and documentation using home scanners or smart phone apps. Third party ID verification made available so that passports and driving licences can be verified online.
Original documents returned to member on day of receipt.	Postal service failures - mail cannot be collected/delivered. Office closures - admin/mail handling staff unavailable to return original documents.	Uploaded electronic documents immediately available to the administration team, cutting out any postal delays/risks. Confirmation of receipt provided through member online services.
Settlement processed and hardcopy confirmation issued by administrator. Lump sum usually in the form of a signed cheque.	Wet-ink signature requirements combined with social distancing and IT security enforcement - prevent/delay disinvestment and settlement of retirement lump sum. Office closures - settlement paperwork cannot be printed/ issued.	Electronic signature and approval alternatives agreed with individual investment managers to facilitate disinvestments. Electronic signature alternatives implemented for secure and controlled authorisation of payments. Confirmation of settlement provided through member online services.

Working in partnership

One gratifying aspect of all this is how readily trustees and members are working with administrators, not just in adapting to new technologies and processes, but also in helping the industry manage the entire production and supply chains. The same community spirit that takes people to their doorsteps each Thursday evening is evident in the absolute lack of any 'me first' attitude – everyone just understands that these are very difficult times.

In our own planning, recognising that the usual SLAs may not hold up under the current realities of homeworking, we reviewed all of our different areas of administration work, categorising each task or project on a priority scale to allow us to focus on the core activities (retirements, payrolls, pension increases, death benefits etc) members would be relying on. Again, Barnett Waddingham started from a good position since we have the benefit of integrated UK based systems, all of our staff are laptop users and we already embrace homeworking in the right circumstances. Like everyone else though, lockdown meant we were working from home, whether the circumstances were right or not.

Our priority list was shared with trustees very early on and made publicly available through a non-secure area of our website dedicated to our Covid-19 response. Without exception, we found that trustees were absolutely on-board with the basic principle of prioritising core services to all schemes rather than all services to their own scheme.

It's a very similar story in discussions with members - rather than the low-level panic or pushback the industry had anticipated once member attention turned to their pension schemes, we've been hugely struck by how reasonable and accepting members are being. Individuals appreciate the efforts administrators are making and, in these sobering times, most members are very willing to adjust their own expectations as long as the scheme and team are open with them.

***Julie Walker APMI DIEB**, Principal and Senior Pensions Manager*

BARNETT WADDINGHAM

Barnett Waddingham is proud to be a leading independent UK consultancy at the forefront of risk, pensions, investment and insurance. We're a team of over 1,200 people (including 73 partners and 119 associates), each delivering on our values and our promise to ensure the highest levels of trust, integrity and quality. We act for a wide range of clients, large and small, in both the private and public sectors including 15% of FTSE350 firms with a DB scheme.

Everything we stand for at Barnett Waddingham is embedded in our promise – to do the right thing. We've applied this meaningful principle across all aspects of our business with continued success. Our continued and long-term commitment to delivering value is our promise to all our people and clients.

We offer a full range of services to trustees, providing tailored pragmatic and proactive advice and support in all aspects of pension scheme management, administration, funding and investment strategy.

Engagement implications of the COVID-19 pandemic

Vicki Bakhshi, Director, Responsible Investment, BMO Global Asset Management

The global coronavirus pandemic is an unprecedented global crisis. The human, economic and financial impacts have already been huge, and it is not yet clear how quickly the virus will be brought under control and normal economic activity can resume.

BMO Global Asset Management's Responsible Investment team has been considering the impact of the coronavirus on the ESG agenda. We are co-operating with other investors to provide companies with a united message on our expectations of how they should respond – we have co-signed the Investor Statement on Coronavirus Response[1] and would encourage other investors to do the same.

With the rapidly-developing situation, we are still in the early stages of understanding the impact that COVID-19 will have. However, some important implications are already emerging that we have set out below.

Company attention to sustainability issues

Our engagement is aimed at elevating the importance of sustainability issues at companies, and where possible, at getting Board-level attention focused on them. With companies rightly focused on the immediate crisis, it is likely to be difficult to get Boards to spend time on sustainability topics.

Our engagement will be respectful that priorities have changed, but we will also aim to ensure that sustainability issues are not forgotten, and that companies continue to make progress where they can. Even in a time of short-term crisis, we need to keep our eyes on the long-term investment horizon.

Although in-person meetings with companies are not currently possible, we are otherwise continuing to engage as usual including through video conferencing and phone calls, in line with our engagement priorities set out at the start of the year. We fully understand, though, that some companies may not have the capacity at present to discuss ESG issues with shareholders. At the time of writing, we have had one company inform us that they are postponing all non-essential shareholder dialogue, and we expect others will follow.

Impact on staff and wider stakeholders

Social issues have often been perceived as the most challenging of the three ESG pillars for investors to understand and make progress on. But COVID has brought social issues firmly to the fore. We have already seen that companies which have put the most effort into progressive policies, such as flexible working, have built greater resilience to weather the current storm.

Addressing employee concerns over sick leave, quarantine and caring responsibilities has been an urgent priority. Some companies have acted responsibly, such as US firms putting in place more generous sick leave provisions above the statutory minimum, and other firms providing mental health support services for staff. Significant gaps between treatment of staff are already apparent, with social media quick to pick up on those companies failing their staff in this time of crisis – a notable example being Wetherspoons, which came under fire for suggesting their workforce seek jobs at Tesco after they abruptly stopped paying wages.

Companies also have responsibilities towards stakeholders, including their suppliers and customers. Helping to alleviate the strains these stakeholders face is important for maintaining relationships in the longer term. Positive measures taken so far include ensuring suppliers are paid on or ahead of time; making products more accessible to vulnerable customers; and philanthropic activities to support affected communities.

Company Annual General Meetings (AGMs)

With mass gatherings banned across the world, in-person company AGMs are no longer possible. Companies have had to cancel or postpone meetings, move to a hybrid (part physical, part virtual) AGM, or where permitted, a virtual online-only AGM.

Although fairly commonplace in the US, virtual meetings are largely a new phenomenon across Europe and subject to legal challenges in certain jurisdictions, where companies are obliged to offer the option of in-person attendance.

1 http://domini.com/covid19-statement

Some countries have temporarily waived this obligation to allow for virtual AGMs, including the UK and Germany. But faced with legal and logistical challenges, some companies have decided to delay or cancel their AGMs, with over 1,250 meetings already postponed at the time of writing. In these cases, dividend payments and capital raising authorities, which require AGM approval, may be delayed.

In normal circumstances, virtual meetings are not popular with investors, as they undermine opportunities for interactions between shareholders and Boards. NGO ShareAction estimates that two-thirds of FTSE100 companies have failed to give shareholders a chance to interact with the company at their virtual AGMs[2]. Companies using this option should ensure where possible that there are still opportunities to allow shareholders to ask questions to the Board.

Executive pay

Executive remuneration has become a sensitive issue as companies are forced to shut down operations, furlough staff and suspend dividends. Shareholders will not generally look favourably on executives receiving generous bonuses following a year where staff and shareholders have lost out.

Some executives have voluntarily taken pay cuts, particularly in highly-impacted sectors such as leisure and tourism, including the bosses of Disney and Royal Caribbean both forgoing their base salaries this year. CEOs able to make these gestures in extreme circumstances are likely to engender greater staff loyalty in the longer term.

However, we recognise that remuneration committees may adjust schemes to permit rewards to executives who demonstrate exceptional skill in navigating their company through the difficult period ahead. We will pay close attention to individual company circumstances, including whether companies are consistent in their treatment of staff and executives.

Capital Allocation

One of the central pillars of corporate governance is where companies decide to focus their funding, with share buy-back programmes a popular choice in recent years. At a time when balance sheets are under immense pressure and companies face significant unexpected costs, management should review the appropriateness of these programmes. Although certain sectors will receive government assistance, the most likely outcome for distressed companies will be the use of emergency capital raising through deeply discounted rights issues or placings. We encourage companies to minimise the dilution of existing shareholders by honouring their pre-emptive rights and giving them the right to purchase further shares before others in the market.

Climate change

Headlines highlight how economic and social shutdowns have caused a decrease in greenhouse gas emissions. However, this is only temporary, and there are other worrying implications of the pandemic on climate change.

The postponement of the COP26 meeting risks a reduced sense of urgency around the climate change agenda, in what was supposed to be a critical year for progress. It is even more important, therefore, for investors to take action, calling on companies to align business strategies with the Paris goals, and encouraging governments to set ambitious national emissions targets.

The International Energy Agency also warned that the economic slowdown is likely to stall many government-funded green projects, as governments urgently divert resources. Meanwhile, collapsing energy demand will negatively impact private sector investment. However, there are now calls for any post-virus fiscal stimulus to have a green element to it, and this 'green stimulus' idea is gaining political traction, particularly in the EU.

2 https://shareaction.org/two-thirds-of-ftse100-agms-shut-out-shareholders-amid-covid-19/

Public health

Pressure on healthcare systems has reinforced key issues such as antimicrobial resistance and access to medicine strategies. Although ineffective against the virus itself, antibiotics may be used to treat some complications, including pneumonia. But poor stewardship in healthcare and farming practices has led to increasing antimicrobial resistance. Vulnerable patients may be at increased risk of worse clinical outcomes and death from this pandemic, and from those in the future. It's therefore paramount to continue effective, cross-sector engagement to address this issue.

In relation to access to medicine and responsible drug pricing, COVID-19 highlights the need to ensure that vaccines preventing infectious diseases, as well as effective treatments, are affordable for all. Public health systems are under huge strain, and companies must work constructively with governments to ensure equitable access to treatment is possible. While some companies have been commended for offering material to help essential coronavirus research, others are accused of profiteering by demanding high prices for potential treatment solutions. Company reputations are at stake perhaps now more than ever, as how they respond in this time of crisis is watched closely.

Conclusion

Beyond these impacts, which range across the ESG pillars, the crisis reminds us that all of us – individuals, investors and companies – have wider responsibilities toward society. The response to, and recovery from, COVID-19 calls for a more sustainable form of capitalism, of the type that responsible investors had been advocating for years. Ultimately, although the crisis will cause some disruption and delay to the 'business as usual' engagement and proxy voting activities, it underlines that the consideration of ESG issues is not just an investment fad, but something which is here to stay.

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Vicki Bakhshi, *Director, Responsible Investment, BMO Global Asset Management*

BMO Global Asset Management

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By providing market-leading investment capabilities across multiple asset classes, we focus on innovating and delivering investment solutions for clients. Today we manage assets in excess of £207bn for a diverse client base, including 500+ UK Pension Schemes (as at 31 October 2019).

We are dedicated to pursuing growth in a responsible and sustainable manner. For over three decades, we have taken a leadership approach in developing sustainable investment solutions. Since launching the UK's first ethical strategy in 1984, our offering has broadened to include a range of ethical and thematic strategies, as well as a comprehensive approach to engagement and voting. In 2000, we launched our flagship reo® service which continues to be a market-leading engagement overlay service.

Coronavirus (COVID 19): the real test for Master Trusts?

Anish Rav, Head of Client Strategy, Atlas Master Trust

These are unprecedented times and the pandemic has given each of us a new and valuable sense of perspective – nothing is more important than health and I hope you are all staying safe.

However, for our industry the ability for schemes to continue to operate and protect their member interests, at a time when members and employers need them most, is critical. This is especially true of Master Trusts which look after many members and control significant assets.

For employers running their own DC scheme, this might be one crisis too many. The world is going to be a very different place when we come out of this situation, working practices are unlikely to go back to 'normal' and businesses will have to adapt to the 'new normal'. Against this backdrop, employers may decide that the time has come to pass on the increasingly onerous and usually thankless responsibility of running the pension scheme to a Master Trust, with all its significant resource and expertise at its disposal. This will allow employers to focus on running their core business, save cost, free up valuable resource and ensure members get the best possible outcome.

To this end, Master Trusts should see greater demand for their services. However, they will need to demonstrate that they were actually up to the job when it really mattered, providing strong evidence that they had the expertise, resource and infrastructure to cope and maintain good levels of service and support, with all the necessary processes and tools in place to cope with disaster recovery on an unimaginable scale.

Some of the key areas that are likely to be looked at are:

Governance

Those of you who read my article in April's edition of Pensions Aspects will know that I am a big advocate of putting Governance at the heart of everything that Master Trusts do, and this situation reinforces that.

A big advantage and selling point of Master Trusts is that they have the knowledge, skills, resources and economies of scale that many single employer schemes do not. It therefore follows that they should be better equipped to provide support to those who need it. Some questions to consider are:

- How have Trustees reacted and have they shown that they are actually in control of the Master Trust?
- Did the Trustees show leadership? Were they able to convene and make the critical decisions at the right time?
- Was the leadership that was provided effective and pro-active?
- What support was given by the Strategists, Funder and Management Team?
- One particular, but sad area to consider is the payment of discretionary death benefits and how this has been handled at a particularly sensitive time.

Business Continuity - Did the plan work?

For many schemes, this is the first time that the business continuity plan has had to be activated and a chance to see how the preparedness worked in real life. The move of the plan from paper to real life must have been effective, otherwise it will have failed. For Master Trusts, their ability to execute the plan will no doubt be critically assessed when employers are deciding who to choose as their Master Trust partner. Key considerations include:

Communications

Member engagement rightly has a strong weighting attached to it when considering the capabilities of a Master Trust, and this crisis has reinforced how critical communication is.

Master Trusts have been praised for their investment in digital engagement and modelling tools for members. Certainly, one of the big advantages they have over single employer schemes is their ability to invest in this part of the proposition.

The ultimate test however is whether members can get access to information and support at the time they need them most. At the most basic level this means being there to allay members fears, reassure them and provide helpful guidance. How schemes interacted with members will become a key factor when considering moving to a Master Trust. For example:

- Was the Master Trust able to keep member helplines open and if not, how long was the delay?
- Were other channels of communication (email, post) kept open?
- What additional support was provided to members (e.g. webinars, newsletters)?
- How quickly did the Master Trust identify the groups that needed most support (e.g. those in drawdown or property funds) and how quickly were they communicated to?

Equally participating employers have needed extra help. Similar questions will be asked about the support provided to them and the flexibility that was given to allow them to meet their legal obligations in challenging financial times.

The future for Master Trusts?

The impact of the crisis is going to have far reaching consequences for years to come:

Short term considerations

In the short term it is likely that projects such as bulk transfers will need to be more carefully planned and executed than ever before, with agile decision making mechanisms in place, ready to deal with any issues that arise at short notice. All parties will need to work together to ensure any changes to agreed plans are clearly communicated and individuals are not left in the dark.

Employers are also likely to pause work on moving active members to a Master Trust as they deal with more pressing employee matters. After all, starting an employee consultation to move pension schemes at this time would rightly be seen as insensitive and low priority.

However, employers will be considering what they can do to adjust to the new circumstances. A quick win for many with single employer schemes will be to move deferred members into a Master Trust. This has many advantages including immediate cost savings, allowing focus on active members and a 'dipping of the toe' into Master Trust.

Master Trusts themselves will need to deal with the consequences of the economic downturn and the impact (if any) that it will have on their business plans. They will also need to consider what adjustments they need to make to their operating model to ensure members and employers receive the service they deserve as well as meeting all legislative requirements.

Long term considerations

In the longer-term Master Trusts will need to learn the lessons from the pandemic and ensure these are considered when developing their governance structure, operating model and strategy. They will need to consider whether they really had the levels of control necessary, what worked, what didn't and the changes that need to be made to ensure they are even better equipped to deal with future emergencies. They should work with all stakeholders and undertake an in-depth analysis of how they reacted, devoting adequate time and resource to this.

From an investment perspective the debate about using illiquid investments in default funds will no doubt be raised – the gating of most property funds has shown how liquidity can become an issue. If there is not enough short-term liquidity, schemes could quickly have cash flow issues. Master Trusts scale should mean they are better equipped than most to use illiquids in defaults, but that debate is for another day.

For many there will be a recognition that Master Trusts are better placed to deal with future crises than single employer schemes, as they have access to a much larger pool of resource and expertise. Employers will want to focus on the day to day to priority of running their business and recovering from the economic fall-out. Switching to a Master Trust is likely to be an attractive proposition which will lead to immediate benefits including cost saving and freeing up resource. However, before they agree to such a move they will (and should) ask one fundamental question:

How did the Master Trust react to the pandemic?

***Anish Rav**, Head of Client Strategy, Atlas Master Trust*

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Wide will wear, but narrow will tear

Oliver Topping, Senior Associate, Sackers

Preparation, adaptability and a broad focus on legal issues are lessons for the pensions industry to take away from the first months of the coronavirus outbreak.

In just a few months, pension schemes have transformed the way they operate. Virtual trustee meetings, administration teams working from home, unprecedented volatility in the financial markets – all parts of the pensions industry have needed to adapt, and adapt quickly.

While the crisis is by no means over, the "new normal" is beginning to settle in, and it's a good time to reflect on how schemes have successfully navigated the first wave of the outbreak. In particular, how can we apply our recent experience to legal and governance challenges arising over both the longer term and also in the immediate future with its unparalleled economic uncertainty?

Preparation and planning

Though no one predicted the impact of the coronavirus outbreak, schemes with comprehensive business continuity plans adapted quickest to the changing circumstances.

Preparation never stops, and schemes should keep their risk registers and continuity plans under regular review, anticipating and managing risks as they arise. These might include the impact of a prolonged economic downturn on scheme funding and covenant, with delays pushing back schemes' endgame planning, as well as knee-jerk member behaviour leading to higher risk of pension scams and poor investment decisions.

Where there are projects needing to be progressed, it is sensible to make use of advisers' experience to pre-empt practical obstacles. For example, arranging for deeds to be executed during the coronavirus outbreak can pose difficulties in practice. Planning in advance can make the process much easier, and avoid last-minute panic.

An interruption in our normal routine can be a good opportunity to take a step back and gain a clearer sense of purpose. Some trustees are finding that the outbreak has given them the time to take back control from their advisers, deciding what goes on the agenda and which projects should go ahead or be delayed.

Preparation isn't just about avoiding negative outcomes. There will be opportunities for schemes in unpredictable times, and schemes should not shy away from identifying and leveraging them to improve member outcomes. The end of the outbreak may transition quickly into capacity constraints as project work restarts and trustees should plan to be ready to move quickly where opportunities arise. Scoping projects properly and a focus on outcomes will ensure that proper resource can be allocated at the right time.

Adaptability and agility

Developments during the coronavirus outbreak have come with relentless speed. It can be easy to be overwhelmed by the volume of guidance from regulators and advisers.

As the outbreak progresses, trustees should ensure that they have put in place appropriate governance structures to quickly adapt to the changing landscape. TPR's easement on quoting and paying transfer values has helped a number of clients manage strains on their administration processes during recent months, and we may see more helpful measures coming through as we approach the summer. A temporary working group could be tasked with keeping a watching brief for updates which could affect the scheme, which could be disbanded when the outbreak is over. A working group could also lead any engagement with the employer where a rapid turnaround is needed, like assessing the implications of furlough on scheme members.

New technologies continue to be adopted by schemes at a fast pace. Could schemes make changes which would benefit them both now and in the longer term? At a time when it is more difficult than usual to certify and post identity documents, we have seen clients investigate online verification services to smooth out administration and keep processes running. Another client has run their MNT ballot partly by telephone rather than post to minimise the need for members to leave the house.

Adaptability also involves focussing resource where it is needed most. When systems are strained, administration teams may need to prioritise key tasks – such as putting new pensions into payment – over less urgent matters. A close relationship between trustees and their administrators, and an understanding of the risks involved in postponing lower priority matters, will help focus discussions and help minimise legal risks.

Broad focus

Schemes mustn't lose sight of the wider picture when dealing with the coronavirus outbreak. The industry has pulled together impressively to keep things moving, but any change can involve a level of risk including from a legal perspective.

While video-conferencing technologies have become popular, trustees should bear in mind that their meetings still need to be held in accordance with the scheme's governing documentation and changes may be needed to ensure that decisions have been validly taken.

Home working has allowed many to respect social distancing measures but trustees should bear in mind their data protection and cyber security obligations and, as and when time permits, ensure that their contracts and policies reflect and formalise steps which have needed to be taken. For example, one client's administrator has rerouted calls via its US servers to allow the administration team to answer calls remotely. Here, the client checked what impact that would have on its responsibilities under data protection law.

Finally, though TPR has introduced some easements in the way it will enforce breaches of pensions law during the outbreak, trustees should still be mindful of their legal obligations which will continue to apply. Advice should be taken where trustees are considering relying on TPR's easements (like suspending the quotation of transfer values) and decisions should be clearly minuted, to minimise the risk of a challenge in the future.

A broader focus, alongside good preparation and an openness to adapt will go some way to helping schemes weather the coming months of uncertainty.

***Oliver Topping**, Senior Associate, Sackers*

Sackers is the UK's leading specialist law firm for the pensions and retirement savings industry. Over 60 lawyers advise pension scheme trustees, employers, corporate investors and providers on all aspects of their UK pension arrangements, including finance and investment, regulatory and ESG, disputes and governance issues as well as corporate pension strategy. We have been consistently ranked as top tier for pensions by the legal directories for over 20 years and were named as pensions law firm of the year at the 2020 Pensions Age Awards.

Best pension practices during the COVID-19 pandemic

Duncan Watson, CEO - EQ Paymaster at Equiniti

At the beginning of 2020, few people expected the new Coronavirus to become a global pandemic that would close businesses, shut down schools, and leave millions of people locked down in their homes. Since then, life as we know it has changed. And for the moment we still don't know when it will return to anything resembling "normal". It's a traumatic time, not least for pension scheme members who may be struggling financially due to the lockdown, and are bound to be panicked by stock market dives and talk of a global recession.

Younger members need reassurance that their life savings are not going to evaporate. And pensioners want to know they can continue to count on the payments they need to survive. So, it's up to pension scheme administrators to overcome the challenges involved in delivering effective services to clients and members remotely.

Overall, the aim is to maintain frontline services such as paying pensioners, getting new pensioners into payment, and handling bereavements, while keeping scheme members informed of the latest developments.

Clearly, technology has a big role to play in this.

Here at Equiniti, for example, we have introduced systems that allow our telephony operation to work from home and be available to answer customer queries. But, as the Pensions Administration Standards Association (PASA) says, "*in these extraordinary times, making sure pension schemes deliver promised income to members is what matters most*"[1].

According to PASA, administrators' priorities should therefore be that:

- Pensioners continue to be paid.
- Cashflow is managed.
- Retirement and death cases are processed.
- Contribution payments are invested.
- Disinvestments are timely.
- Pension increases are calculated.
- Members have appropriate communication.

Here, we take a closer look at how these priorities can be met, according to three key groups.

Priorities for pensioners

Pensioners who rely on regular payments from the scheme to live are the most vulnerable category of members at this time – especially as many of those over the age of 70 are isolated from their families and friends.

Administrators must therefore ensure that they receive an uninterrupted income; in other words, the pension payroll has to run on time. This means reviewing the cashflow policy to make sure it remains sufficient for both investments and disinvestments. In the event of a scheme member dying, meanwhile, the challenge is to remain sensitive, while ensuring any death benefit is quickly settled.

PASA's guidance suggests this may mean altering protocols for agreeing discretionary benefits during lockdown. It also urges administrators to harness the power of technology to both drive member engagement and meet best practice requirements by, for example, moving away from wet signatures and making electronic payments mandatory.

Priorities for those approaching retirement

Workers preparing to retire from defined contribution schemes are among those worst hit by the current market losses – mainly because they lack the time for markets to go up again.

Administrators should therefore offer information on the options available to give their funds a chance to recover.

These include:

- Delaying retirement.
- Drawing out a small amount of cash rather than committing the whole investment.
- Living off other savings for a while.

For those retiring from a defined benefit scheme, meanwhile, the recent stock market falls do not have a direct impact – although they may well put extra strain on the pension fund as a whole. That's why the Pensions Regulator has told employers they can put payments into final salary pensions on hold where absolutely necessary and given them the

1 Covid-19 Guidance for Administrators, PASA, 2020

ability to delay member requests to transfer out of the scheme for up to three months.

The regulator's main aim is to prevent businesses going under due to mushrooming pension scheme deficits. However, delaying kneejerk transfers also helps mitigate the risk of members making poor financial planning decisions in response to the crisis situation, or being taken in by scams.

Other ways administrators can protect all members from fraud include encouraging the use of secure websites or an encrypted message system for any correspondence, and warning any employees working remotely to also be on the look out for "phishing" scams.

Priorities for active members

For defined contribution scheme members with the time for their funds to recover from the current situation, right now doing nothing is probably the safest policy.

PASA's advice includes reassuring final salary scheme members their benefits are secure. It also involves providing information on long-term investing for those in defined contribution schemes – either via a member portal or as a separate exercise.

Some members may, however, want to take advantage of the market falls by increasing their contributions – especially with the Bank of England base rate now offering savers returns of just 0.1%.

And others may be keen to reconsider the risk profile of their investment allocations.

Making such actions possible should, therefore, also represent a priority for administrators at this time – especially as interactive member portals can be a great way to boost engagement overall.

According to a recent current accounts' report from the Competition and Market Authority (CMA), "annual interest statements have virtually no effect on consumer actions. But given immediately actionable information – text alerts and internet banking – overdraft charges can be reduced by consumers by almost 25%"[2].

The same is true for pension scheme members.

Giving them the power to make even small changes can make them feel much more involved. And for those under pressure to reduce or stop their pension contributions due to the financial strain of lockdown, having access to retirement income modelling tools that show the impact of reducing or stopping their contributions may encourage them to keep saving where possible.

Other ways to support this group include communicating details of the government aid available. Plus, highlighting money-saving employee benefits such as discounts and tie-ins with partners such as insurers and utility providers – as well as relevant services such as will writing and online GP consultations.

Finally, with the pandemic raising stress and anxiety levels for many, it is worth taking steps to avoid employees feeling isolated, and to promote any mental health support available via the benefits programme. *"Poor mental health affects productivity and accuracy,"* PASA says. *"Therefore, employee wellbeing can't be ignored."*

***Duncan Watson**, CEO - EQ Paymaster at Equiniti*

EQUINITI

Equiniti Group plc, an international technology-led services and payments specialist, provides non-discretionary payment and administration services to some of the world's best-known brands and UK's largest public-sector organisations. It is the UK's leading provider of share registration, employee share plans, and associated investor services, and also has market leading positions in pension administration and software, and employee benefit schemes.

2 Retail banking market investigation, CMA, 2016

COVID-19 and Master Trust providers

Shabna Islam, DC Consultant, Hymans Robertson
Michael Ambery, Partner and Head of Provider Research, Hymans Robertson

The COVID-19 (coronavirus) pandemic has been completely unprecedented in terms of speed and scale, and the containment measures deployed to slow the spread of the virus. For both Master Trusts and their members, COVID-19 poses significant risks and challenges.

For most schemes, priorities will relate to resolving any immediate, practical business continuity issues around paying benefits and getting the governance in place to support ongoing decision-making. Thereafter, what will business as usual look like in an environment that is socially distanced, at least for a time? And how does that then return to normal? Will that normal be impacted by what has happened during this period? And, what then should be the focus for Trustees and governance boards, both short term and in the longer term? We look at several key areas - what we know so far and what you should be considering:

Key area	What we know so far?	What should you think about?
Administration	Master Trust administrators have seen a slight increase in calls and even complaints regarding investments due to extreme market volatility. We are aware of an increased number of calls to employer HR and payroll teams to query whether contributions can stop and how best to ride the volatility. Following lockdown, providers saw a fall in call volumes – we believe members were prioritising other essential activity. Most providers were able to retain open helplines, whilst call handlers were redeployed to work from home, prioritising 'vulnerable' customers. The expectation is for call volumes and activity to increase in the coming weeks, following the impact of furloughing of staff, and as regular member communications (e.g. annual benefit statements) are issued. Members may well opt out of the pension scheme all together and undo the success of Automatic Enrolment. Master Trust providers, where necessary have been prioritising the processing of death claims, ill-health claims and retirements.	Have there been changes in member behaviours which have impacted the number of opt outs, early/ late retirements, transfers in/out, changes in pension contribution levels and investment switches? How are communications able to give confidence to members and assist in their decision making? Have core administration processes, such as processing of pension contributions and payments, continued in line with Service Level Agreements and data security protocols? Is there any impact on how death claims are processed? Are you clear on how the administrator will prioritise any increasing workloads and the treatment of 'vulnerable' members? Does the pension benefit link with other benefits such as group life benefits and how have claims and policies been impacted?

Key area	What we know so far?	What should you think about?
Member communication	Master Trust providers have made available helpful guidance on the impact of COVID-19, including the significance of recent market volatility, on members' pension income. Information has been provided on dedicated websites pages, rather than direct emails or mailings, thus avoiding an inadvertent kneejerk reaction. Providers have been keen to direct members to online support so freeing up helplines for the most vulnerable members. Providers are keen to work with sponsoring employers to formulate a tailored and targeted approach to any specific needs for further communications to members. E.g. furlough of staff.	Should the provider's communications be supplemented by additional communications? This could cover: the wider financial wellbeing support available to members, increased risk of pension scams, a reaction to changes in member behaviour and information on restrictions placed on particular investment funds. If there was the need to issue urgent member communications, is this possible? Are all members contactable by email? Are you clear on the implications of furloughing staff, and the impact on pension contributions?
Investment	With extreme market volatility, not all Master Trust default funds have performed in line with expectations. Many property funds have been frozen due to the difficulty in obtaining valuations. Whilst death and retirement claims can continue to be processed, this freeze poses challenges for other planned activity.	Assess the impact of market volatility on the default fund and lifestyle switching – are members locking into losses? Does the default investment fund need to be reviewed? Are any planned strategic investment changes still appropriate in the current climate? What are the challenges of funds being frozen, and how significant are they? How do you communicate this to members? Have market movements created possible investment opportunities?

Key area	What we know so far?	What should you think about?
Governance	Master Trust Trustees have played out their business continuity plans, but no provider was fully prepared for a pandemic. Pandemic plans have or are being put in place and succession plans are being reviewed.	Is the Master Trust board running as close to business as usual as possible? Is there a key person risk to manage in the unfortunate case an individual becomes ill? Can enough people sign documents if required? Is an electronic / scanned signature adequate? Will there be disruption to planned projects / should any projects be put on hold? Are there any regular or statutory deadlines to manage (Chair's statements, accounts, annual benefit statements)? And are these on track?
Appointment risk	The expectation is that larger well-established and diversified pension providers will see through these unprecedented times and in some cases come out the other end stronger. Some smaller providers are expected to become distressed leading to a potential takeover by larger providers. This will accelerate the rate of consolidation in the market.	How have Master Trust providers, their advisers and sub-contractors implemented working in lockdown conditions? How may COVID-19 affect demand, supply (staff and resources) and cashflow? Is the wider business in a particularly affected sector? How is the provider measuring the impact of the downturn and planning for further extreme scenarios? Does the structure of the provider/owner of business affect this? Are you as ready as you could be for the possibility of the provider entering insolvency? Are planned product innovation spends being reviewed/put on hold?

Key area	What we know so far?	What should you think about?
Transitions	Given the extreme market volatility, Master Trust providers have in general reduced their pre-funding levels for any transition projects, thus increasing the out-of-market risk for members. Given the increase risks, providers have a preference to defer transition work. The expectation is pre-funding levels could be reviewed upwards by deferring. With closure of property funds, this adds a further layer of complication to transition projects.	Should any transition projects go ahead, or should they be postponed? Have you documented the reasons to proceed or postpone? Do you have an approach to deal with the challenges of a transition in the current extreme climate?

Governance Committees, Trustees and Employers all have a lot to think about. We suggest seeking and sharing information from your provider and obtaining advice on best course of action. We also suggest, where appropriate, considering the impact of the current environment on members and the sponsor employer. Alongside that, the actions of members with providers and payrolls should be closely monitored in order to provide communications that are supportive.

In such unprecedented times, we would like to praise providers and pension professionals in being able to invoke on disaster recovery and business continuity plans. Our thoughts are with everyone in what has been a challenging time and as things return to normal, we hope that the suggestions regarding what considerations and actions that can be taken now are brought into current and future business planning.

Shabna Islam, *DC Consultant, Hymans Robertson*
&
Michael Ambery, *Partner, Hymans Robertson*

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Investing in extreme conditions: using synthetic exposures to overcome the liquidity conundrum

Jos Vermeulen, Head of Solution Design, Insight Investment

It has been an extremely turbulent period, and pension schemes have felt the impact of extreme volatility across asset classes.

Investing in this environment presents a dilemma for schemes seeking to ensure they have sufficient liquidity, while investing to improve their funding level. One potential solution may be synthetic exposure.

The crisis has hit pension schemes hard

The economic impact of measures to contain the coronavirus will be severe, and markets have responded sharply, with rapid declines in liquidity and extreme volatility.

This has had clear negative implications for UK defined-benefit pension schemes. Scheme assets have shrunk in value while liability valuations have grown. The aggregate funding ratio of schemes has fallen from 98% to 92.5% over the first three months of 2020, reflecting an increase of over £100bn in their aggregate deficit, according to Pension Protection Fund data.[1]

The dilemma for pension schemes

The crisis presents pension schemes with a dilemma. Many are maturing, paying out more in pensions than they receive from investments and sponsors. In the current environment, sponsors may be less able to spare the cash to support their schemes – which may therefore wish to emphasise having enough liquid assets.

However, for schemes with meaningful deficits and a conviction that markets are too negative about the economic outlook, investing for growth to improve long-term solvency is an appealing prospect.

This dilemma – whether to hold a prudent allocation to liquid assets but miss out on potential growth, or to invest in return-seeking assets but risk being caught out in another liquidity squeeze – is difficult to resolve.

Synthetic exposure could help schemes retain liquidity and invest for growth

One potential solution is synthetic exposure: using derivatives to gain market exposure without buying equities or corporate bonds.

This can:

- free up capital while retaining exposure to markets, and
- allow schemes to prepare for long-term strategic changes without committing additional capital.

Pension schemes looking to free up liquidity could sell equity holdings and replace them with a total return swap: the scheme pays a regular amount – for example, an interest rate plus a margin – in return for payments that rise and fall in line with an equivalent basket of equities (usually an index). Alternatively, they could use futures.

Transitioning to synthetic exposure means freeing up capital without realising losses. The capital may be used to fulfil cashflow obligations and/or to top up their overall collateral pool. (Investors should note they need to hold some collateral aside to cover mark-to-market moves in the value of their exposure.)

For schemes seeking to increase their long-term strategic allocation to corporate bonds, they could take the next step using synthetic credit exposure.

Investments in high-quality credit assets, held to maturity, are attractive as they can offer contractually defined income streams and higher certainty over potential returns. Large-scale corporate bond allocations can also help to immunise schemes from changes in the pricing of pensioner buy-outs.

For pension schemes underweight credit relative to their strategic objectives, synthetic credit exposure using credit default swaps (CDS) can help to change their allocation in line

1 https://ppf.co.uk/ppf-7800-index

with their targets. CDS allow investors to pay a premium in return for the promise of a payment if a borrower defaults on their debt. CDS pricing typically changes in line with associated bonds, so selling CDS can help investors build desired exposure to corporate bond markets quickly and easily when the time is judged to be right.

When capital comes available, a scheme can then transition into corporate bonds – the hope being that selling CDS will have acted as a proxy hedge for changes in credit spreads, making the implementation of the longer-term strategy more affordable.

Conclusion: no need to pause your long-term strategy

Before the pandemic, a consensus was emerging that a prudent strategy for a typical pension scheme involves hedging liability risks, investing to achieve required growth, and managing liquidity to achieve long-term targets while also fulfilling short-term cashflow obligations.

Recent volatility has tested investors, but these strategic principles remain sound. Synthetic exposures could help improve your strategy without having to compromise. Liquidity can be maintained or improved, while capturing strategically consistent opportunities.

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***Jos Vermeulen**, Head of Solution Design, Insight Investment*

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We also work with our clients to successfully navigate defined benefit endgame options. Some pension de-risking options may appear attractive, but in reality they may make it more difficult to reach the endgame.

We can help pension schemes reach a buy-out with greater certainty by:

- considering the value for money of each de-risking option
- assessing the overall risk and return impact on the portfolio
- maintaining flexibility to handle future unpredictable risks

Managing through COVID-19: a fiduciary management perspective

Ajeet Manjrekar, Co-CEO River and Mercantile Solutions

We have been providing fiduciary management services over the last 17 years, including the 2008 Global Financial Crisis. Whilst history can repeat itself, the adage "this time it's different" also rings true in the current crisis. We believe important lessons were learnt from 2008. In particular, heightened uncertainty means we must examine the situation more closely and avoid automated decision making where possible.

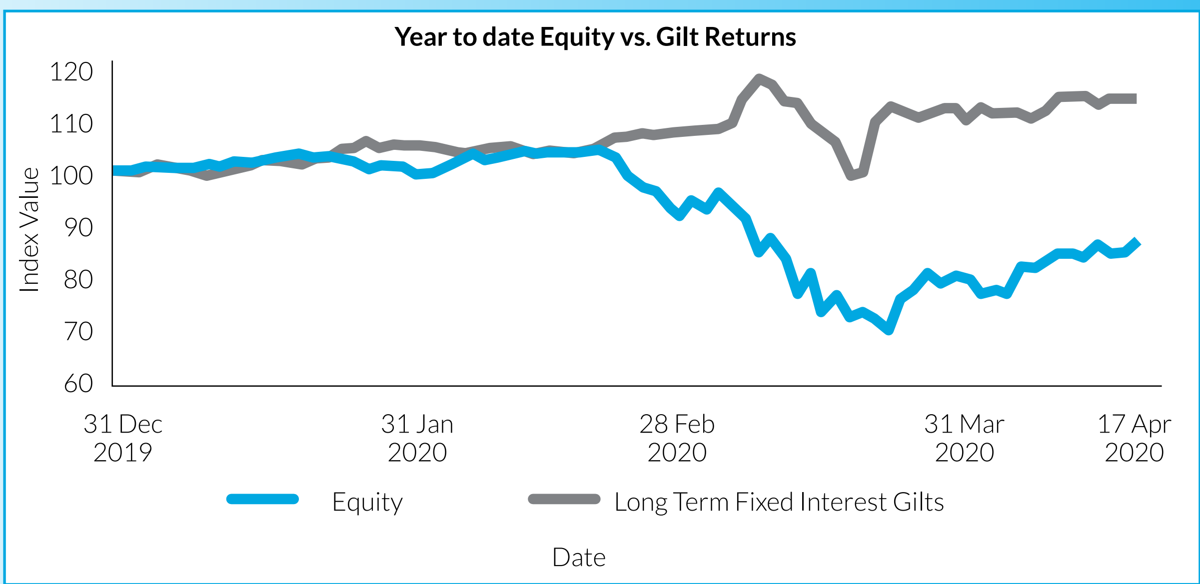
For example, as pension schemes look back on the first quarter of 2020 following one of the most volatile quarters in history, it is likely schemes have drifted from their strategic asset allocation. This flags the question of when and how to rebalance back to target. For some schemes and implementation arrangements (e.g. certain external fiduciary solutions), rebalancing may be an automatic process.

Pension trustees set a strategic asset allocation target aligned to their funding goals. During periods of high volatility or large asset moves, the scheme's strategy may drift away from its target. So it may be appropriate to rebalance the portfolio. But, reflecting on our fiduciary manager experience, we flag four key questions.

What has driven the need for schemes to rebalance?

Equity markets have fallen c.13% this year, with long term UK government bonds moving the same amount but in the opposite direction. A simple scheme starting the year with a strategic target of 50% equity and 50% gilts would now be c. 7% underweight to equities (all other things being equal). A higher starting allocation to equity or the use of leveraged LDI would have resulted in an even bigger imbalance.

But, this is a simplification. Most schemes have a diversified portfolio investing across a range of asset classes. With equities the hardest hit, diversification will have helped. Fiduciary managers may have also adapted portfolios to prevailing market conditions. They may have reduced exposure to equities and other on-risk assets. This will have cushioned the impact of market falls providing some relief. Yet, even with diversification and agile asset allocation, the impact on asset values means many will face a decision on when and how to rebalance from off-risk to on-risk assets.



Source: River and Mercantile Solutions, Bloomberg, 17th April 2020. Date of analysis: 31 Dec 2019 to 17 Apr 2020. Past performance is not a reliable indicator of future results and should not be relied upon.

How should schemes rebalance?

Some schemes may have an automatic rebalancing framework between off-risk and on-risk assets. After a fall in on-risk assets, many academic studies support this approach over the long run. But pension schemes, whilst long-term investors in principle, face several short-term challenges.

Reducing off-risk assets may reduce the level of liability hedging or collateral position. Reintroducing liability risk is not a desirable position for most schemes. Particularly those experiencing a sea of red across their integrated risk management dashboards. With interest rates at low levels, schemes may have to top up their off-risk LDI allocation, should interest rates rise sharply from here.

Fiduciary management solutions using segregated liability hedging (rather than pooled alternatives) offer a distinct advantage at this time. They can operate with higher levels of leverage, providing schemes with far greater flexibility. A segregated approach does not force the scheme to top up their LDI allocation at short notice. Additionally, it means schemes can rebalance into on-risk assets without compromising on liability risk management.

To our mind, a segregated approach represents a more flexible, efficient, and robust solution. Pooled LDI can tie trustees' hands by closing down the options available and increasing the likelihood of depleting cash buffers. With higher transfer value activity and potential contribution holidays, this can put a further squeeze on schemes' liquidity levels.

The enforced shutdown of much of the global economy has put UK pension plan sponsors under severe pressure. The record pace of credit rating cuts, and a junk bond market flooded with 'fallen angels' illustrates the increased credit risk of UK PLCs. Automatic rebalancing could mean re-risking the assets when the Sponsor is most vulnerable. Also, on-risk assets may have further to fall in the months ahead, as the suspension of global productivity feeds through to underlying economies, industries, and sectors. So now might not be the most appropriate time to pull the rebalancing pin?

An alternative approach is to hold cash and short-dated gilts as an interim measure, whilst preparing to invest in emerging opportunities as the market stabilises. This may well be a more robust course of action. Furthermore, maintaining higher cash balances to support cashflow in this time of uncertainty represents many schemes' top priority.

Green shoots appearing, but are we out of the woods yet?

The topic on every (virtual) trustee meeting agenda seems to revolve around the opportunity to "capture the bounce". We are all aware of the re-bound in on-risk assets following the Global Financial Crisis. Will a post-COVID-19 bounce dig us out of the deficit hole which emerged in the first quarter? There may be a tremendous buying opportunity. But timing the entry point will be a challenge. In an environment where market commentators revise their economic growth forecasts down every day, it is important to consider which on-risk assets we would favour.

Headline pricing of certain asset classes such as high yield may look very attractive today. But, as a fiduciary manager, it is crucial to look under the hood. The Energy, Retail, Leisure and Air Travel sectors are amongst the worst affected. So, a high yield allocation should look to avoid these troubled industries. This means a bespoke mandate rather than the benchmark-aware approach of many fund managers. Fiduciary managers can invest selectively to build robust portfolios such that investors are compensated for risks in the current environment.

Illiquid assets: has the day of reckoning arrived?

In times of uncertainty, trustees naturally want to see their latest funding position to communicate with other stakeholders and support effective decision making. But, it is important to understand how up-to-date this information is.

Using illiquid assets can be a useful tool for long-term investors such as pension schemes. But, with these assets valued only once a month or quarter many are yet to be priced based on the latest market information.

Given initial guidance from listed equivalent firms, these assets will very likely need to be marked lower, as the underlying contractual assets and covenants may well be impaired. This risk will increase if the current crisis continues for an extended period.

If a fiduciary manager has a large allocation to illiquid assets, this may result in only "stale" pricing being available. This can lead to an over-inflated asset position, impacting on any asset allocation changes being proposed today.

But, fiduciary managers in the dry powder camp, with liquid assets at the ready, can snap up attractive opportunities at stressed asset prices.

Many lessons were learned from the Global Financial crisis. But whether a Black Swan or a Grey Rhino, this crisis is a very different animal. The nuances of this particular crisis and its impact on the three pillars of pension scheme risk (funding, investment and covenant) must be well understood. Experienced Fiduciary Managers can help schemes navigate these turbulent times – avoiding risks and capturing opportunities. But Fiduciary Management comes in many flavours and trustees must understand how different approaches could restrict their options, or introduce unwarranted risks during periods of market stress. A flexible solution which can adapt as conditions change is the approach we support and adopt for our clients.

***Ajeet Manjrekar**, Co-CEO, River and Mercantile Solutions*

RIVER AND MERCANTILE SOLUTIONS

River and Mercantile Solutions is part of the River and Mercantile Group, a specialist investment firm focussed on delivering client led advice and investment solutions.

Our specialism is in delivering investment advice and fiduciary management to pension schemes. We have the longest track record in fiduciary management in the UK– 17 years for DB schemes, and 9 years for DC schemes.

Our clients were early adopters of liability hedging through our specialist in house team. Our tailored solutions provide more flexibility to target the return clients want, and the level of risk they can bear. The outcome is our clients reach their goals faster and with less risk. It's simply smarter.

Retiring in turbulent times: 10 steps to help members understand their options

Jonathan Watts-Lay, Director, WEALTH at work

The turbulent markets we have experienced due to COVID-19 are concerning for everyone but especially for members of a defined contribution (DC) pension scheme who are looking to retire. Whilst retirement planning is important regardless of the climate, it is particularly crucial when stock markets are volatile.

Experienced investors know that when it comes to stock markets, they are supposed to buy at the bottom and sell at the top. However, not all investors act on what they know when markets unexpectedly drop, as their sense of protecting assets prevails, which often results in knee-jerk reactions such as withdrawing their funds from their investments. It is likely that many employees in DC schemes are not experienced investors and will be tempted to react in a similar way. Employers and Trustees must therefore ensure that their pension scheme members are aware of the risks involved and help them understand their options before they make any rash decisions.

To help with this, we have provided 10 steps employers and Trustees can take to help their pension scheme members who may be concerned about their retirement:

1 Encourage members to put a retirement plan together

Before making any decisions about retirement, members should put a plan together which considers how much income they will need in retirement to meet their day-to-day living expenses (household bills etc.), discretionary income (holidays, hobbies etc.) and how their income needs may change over time. Members may find they are able to adjust their spending in the short-term to compensate for any pension losses such as not buying the discretionary extras.

2 Encourage members to not cash out in panic!

No one knows what is going to happen in the near future, but what we do know is that if members cash out now, they will not only be taking money out of their tax efficient pension but they may also lose out when markets recover.

3 Ensure members understand the tax rules

As well as the risk of potentially selling at the bottom of the market, the other danger of cashing out is that members risk paying a lot of unnecessary tax. Usually only the first 25% of a DC pension is tax free; the remaining 75% is taxed as earned income. By taking their pension as a cash lump sum, not only will they be selling when markets are low but they may end up with a big tax bill!

4 Help members understand their options to delay retirement or work part time

There is every chance that everything will look very different in a few months' time. If members are able to delay their retirement, it may be worth them considering this. It would give some time for markets to hopefully recover, and give them more confidence in leaving the workforce.

5 Encourage members to consider other pensions

The full State Pension is increasing from £168.60 (2019/20) to £175.20 (2020/21) per week. This represents a 3.9% increase - although not everyone is entitled to this so they would need to check their eligibility. For those who may also have a defined benefit pension, the pension income entitlement that has been built up is secure, so stock market fluctuation will not impact the pension income payable at retirement.

6 Encourage members to consider other savings

When it comes to retirement, there are many assets such as cash ISAs and general cash savings, which can be used as potential sources of income in addition to pensions. If members want to give their pension some time to recover, they might want to use these other savings first.

7 Encourage members to shop around

Members should shop around before they purchase any retirement products. The Financial Conduct Authority (FCA) found that those who go into income drawdown could increase their annual income by 13% by switching from a higher cost provider to a lower cost provider. It is important they not only check fees, but make sure it suits their needs, and that they can withdraw cash as and when they want it, and for as long as they need it.

8 Promote the importance of regulated financial advice

Speaking to a regulated financial adviser can reassure members in these concerning times, and can actually cost the same, if not less than buying retirement products, such as annuities, through some online brokers. It can also be seen as an investment as an adviser will look at all assets, work out the most tax efficient way for members to fund their retirement and then put a bespoke plan in place, which will support them throughout retirement.

9 Protect themselves from scams

Unfortunately turbulent times like these, when members are concerned and vulnerable, is often when scammers see an opportunity. It is important for members to be vigilant. Scammers tend to sound completely legitimate and it's easy to see why so many people are fooled, and it isn't small amounts of money which are being taken. Findings from the FCA and The Pensions Regulator show that victims of pension scams could lose 22 years' worth of savings within 24 hours. So, it's vital for members to check whether the company they're planning to use is registered with the FCA https://register.fca.org.uk/. They can also visit the FCA's ScamSmart website which includes a warning list of companies operating without authorisation or running scams www.fca.org.uk/scamsmart.

10 Provide education and guidance

This is the one thing employers and Trustees can do to support members and help them make informed decisions. Financial education at retirement can be delivered in a number of different ways and although face-to-face seminars remain our most popular and effective communication method, this may not always be possible. Therefore, formats such as live online webinars and individual telephone (or indeed video) calls can be an effective alternative. This range of delivery methods can ensure the majority of members are supported whether they work remotely or not and can also ensure a solution for deferred members.

***Jonathan Watts-Lay**, Director, WEALTH at work*

WEALTH at work is a specialist provider of financial education and guidance in the workplace supported by regulated financial advice for individuals.

We deliver tailored financial education and guidance which helps pension scheme members understand the various retirement income options available and key issues such as tax, investment risk and how to create a sustainable income. Our regulated financial advice service helps individuals to understand their personal financial situation whether they're facing investment and tax considerations, or selecting their retirement income options.

This complete service offering helps Trustees support pension scheme members to make informed decisions, in order to maximise their retirement and lifetime savings.

Unprecedented challenges and unprecedented responses

John Wilson, Head of Technical, Research and Policy, Dalriada Trustees

The COVID-19 pandemic has quickly become not only a healthcare crisis but also a financial one, which is unlike any before, including the 2008 'credit crunch', and which requires responses from The Pensions Regulator (TPR) that are equally unprecedented. This challenge has not been lost upon TPR. Already the guidance and easements in its COVID-19 'hub'[1] far surpass the response to events of just over a decade ago[2].

The measures announced span employers, trustees, members and scheme providers. Whilst the impact varies by stakeholder, an overarching theme is that, whilst the legal framework within which workplace pension schemes operate has not changed, TPR will be pragmatic when deciding whether or not to use its powers and impose sanctions.

What then does this mean for those involved in the administration and sponsoring of occupational pension schemes?

Funding, Investments and Transfer Values

One of the first substantive announcements from TPR covered guidance for trustees on defined benefit (DB) funding and investments (including guidance for schemes with employers in distress)[3].

Importantly, it began with the caveat that TPR was *"not authorising, encouraging or compelling a particular course of action - we expect trustees to do the right thing for their situation and members".* The document then highlighted some good practice ideas and outlined TPR's current response to legislative breaches or trustee actions, including:

- Recognition that valuation assumptions will have been set under very different conditions and TPR does not necessarily expect trustees to revisit these assumptions. So, trustees are not required to allow for relevant experience since the effective date of the valuation in their recovery plan, but post-valuation experience should be "considered" when agreeing the recovery plan in the context that the employer's affordability may now be constrained.
- It might be appropriate for trustees to delay submitting their valuation by a short period of up to three months. Trustees are assured that they will not be fined for this, even if statutory deadlines are breached.

Notwithstanding the easements above, the guidance highlights that *"If trustees are ready to complete their valuation now and they think it is in the best interest of their members to do so, they should submit it".* The easements are there should trustees need them and should not be viewed as a licence to delay.

Further information is expected in TPR's 2020 Annual Funding Statement which, at the time of writing, is overdue, with its delay directly attributable to the current pandemic. TPR is acutely aware that sponsoring employers may request easements during such challenging times. Further, trustees may not be able to immediately obtain information to assess covenant and affordability. The TPR guidance therefore includes the following *"good practice ideas"*:

- Where employers make an 'unsubstantiated' request for an immediate reduction or suspension of deficit reduction contributions (DRCs) due to liquidity constraints, this should be limited to the shortest period possible and certainly by no more than three months.
- Employers should commit to providing trustees with all information required in a timely manner.
- Other forms of value leaving the employer covenant should be suspended (including payments to shareholders and to related entities).
- Requests to suspend or reduce payments for future service should be treated similarly.

1 https://www.thepensionsregulator.gov.uk/en/covid-19-coronavirus-what-you-need-to-consider
2 https://webarchive.nationalarchives.gov.uk/20100612130311/http:/www.thepensionsregulator.gov.uk/docs/statement-to-trustees-oct-2008.pdf
3 https://www.thepensionsregulator.gov.uk/en/covid-19-coronavirus-what-you-need-to-consider/db-scheme-funding-and-investment-covid-19-guidance-for-trustees

According to TPR, *"In the absence of clear covenant visibility in the short to medium term, we expect trustees to continue to offer only short-term concessions … Trustees should be mindful of how other creditors are supporting the employer … [they should] fully document their considerations and decisions".*

Regarding their scheme investments, TPR's key message is that trustees should review with their advisers what actions (if any) might be necessary. Considerations include, but are not confined to:

- cash outflows and inflows;
- investment strategy and mandate rebalancing requirements;
- diversification and any concentrations of risk;
- derivative positions and structures held, and collateral management arrangements;
- exposures to certain counterparties; timing of any pre-agreed transactions;
- continued functioning of sub-committees and delegated responsibilities;
- integrated risk management (IRM) policy and monitoring framework; and
- governance structures.

The guidance around funding and investment also covers the issue of transfer values where, in addition to flagging the heightened risk of pension scams, TPR suggests that trustees consider the terms they are offering for cash equivalent transfer values (CETVs) and may decide to suspend CETV quotations and payments for up to three months. In this event, TPR will not take regulatory action against trustees over the next three months. TPR also notes that trustees may want to review terms they offer for other benefit options (e.g. commutation).

"If, at the end of the three-month period, trustees feel it is still in the best interests of their members to continue with the CETV suspension or delayed quotation, they should notify us in the usual way." {The Pensions Regulator}

Reporting duties

Much more recently, but with some overlap in respect of the above guidance, TPR provided an update on reporting duties and enforcement[4].

In the update, TPR states that, if a breach will be rectified within a short timeframe (not more than three months) and it does not have a negative impact on savers, there is no need to report to TPR – but records of any decisions made and actions taken must be kept.

In making decisions about whether to take regulatory action in respect of breaches of administrative and compliance requirements, TPR plans to take "a case-by-case basis and adopt a flexible approach".

There are, however, some areas where TPR will not be using the above guiding principles, or where it is considered useful to provide more detail on the approach. For the following, reference should be made to TPR's COVID-19 hub: *annual benefit statements, chair's statements, charge controls, DB transfer values, employer consultation, employer related investment, investment governance, late accounts, late payments of contributions, Master Trusts, notifiable events, recovery plan not agreed.*

Administration of pension schemes during pandemic

The main message from this guidance[5] is that schemes should focus on key risks to savers: *paying benefits; protecting members from scams; ensuring contributions are paid; and supporting good member decisions.*

Reference is made to the Pensions Administration Standards Authority (PASA) COVID-19 guidance for administrators[6] which is equally emphatic about ensuring sufficient funds are held to settle benefits and other scheme expenditure, maintaining evidenced accuracy for benefit calculations, and keeping good records of any work in progress.

4 https://www.thepensionsregulator.gov.uk/en/covid-19-coronavirus-what-you-need-to-consider/covid-19-an-update-on-reporting-duties-and-enforcement-activity
5 https://www.thepensionsregulator.gov.uk/en/covid-19-an-update-for-trustees-employers-and-administrators
6 https://www.pasa-uk.com/wp-content/uploads/2020/04/COVID-19-Guidance-for-Administrators-March-2020-FINAL.pdf

In its guidance, PASA has identified the 'basic enablers' required to meet pension scheme priorities when remote working. These include planning for the critical tasks of running pensioner payroll / settling benefits, reviewing cashflow to ensure it remains sufficient, moving away from wet signatures, member communication, encouraging use of secure websites and avoiding face-to-face meetings.

Once the basic enablers are in place and priorities are being met, the considerations can move to medium term and 'second order' processes. These could include transfer value requests, issuing annual benefit statements and some ongoing projects.

As to higher level enablers, PASA expects administrators to aspire to adopt best practice for delivering administration services to trustees and members in this current remote working environment. This depends on leveraging cutting-edge technology and supporting processes.

The PASA guidance recommends, in a change to the conventional practice of requiring original certificates to settle benefits that, where possible, administrators should be adopting biometrics or other methods of identification verification avoiding the need to post valuable certificates.

Defined Contribution (DC) Schemes and Automatic Enrolment (AE)

For DC arrangements, it is recommended that trustees review with their advisers what actions (if any) might be necessary to take for their schemes and members. These actions could include[7]:

- Member communications (taking into account different periods to retirement, increased risks of pension scams, importance of advice, free and impartial guidance available from the Money and Pensions Service - MaPS).
- Investment strategy and mandate rebalancing requirements.
- Diversification and any concentrations of risk.
- Exposures to certain counterparties.
- The timing of any pre agreed transactions / fund switches.
- Continued functioning of sub-committees and delegated responsibilities.
- Governance structures.

Separate guidance on employer AE duties during the pandemic[8] observes that these obligations continue to apply as normal, even if staff are being 'furloughed'. On this note, i.e. the Coronavirus Job Retention Scheme[9] and workers on temporary leave (furlough), employers are reminded that claims to cover wages can include statutory minimum AE contributions.

If using a DC pension scheme and the employer contribution is more than the statutory minimum, the TPR guidance notes that it may be possible to decrease it to the statutory minimum. Further, provided certain conditions are met, TPR will not take regulatory action if contribution reductions are not preceded by the usual 60-day consultation period.

The above easement, as with many of the others, applies up to 30 June 2020, at which point it will be reviewed.

Next Steps

At the time of writing, TPR has committed to providing further guidance in the coming weeks and months once there is a better idea of the extent of the crisis, its possible impacts and the package of measures that governments and other organisations intend to adopt.

In the interim, trustees need to understand the potential impacts on their scheme and take proportionate action where necessary. A checklist of possible next steps is provided in the table on the following page.

7 https://www.thepensionsregulator.gov.uk/en/covid-19-coronavirus-what-you-need-to-consider/dc-investment-and-transfer-values-covid-19-guidance-for-trustees
8 https://www.thepensionsregulator.gov.uk/en/covid-19-coronavirus-what-you-need-to-consider/automatic-enrolment-and-pension-contributions-covid-19-guidance-for-employers
9 https://www.gov.uk/government/publications/guidance-to-employers-and-businesses-about-covid-19

Risk Registers	Add 'The impact of Covid19' to scheme risk registers and consider an emergency meeting [held remotely] to discuss its effect.
Business Continuity Planning	Prepare or review business continuity plan (BCP) for the impact of COVID-19.
Service providers BCP	Business continuity should also be checked at a service provider level. Most entities have produced a document detailing their response to the Coronavirus and trustees also need to understand service level agreements and which scheme activities would be prioritised in the event of under-resourcing.
Governance	Internal controls / policies should be put in place to ensure decisions can still be taken when trustees cannot meet in person and / or some trustees are unavailable due to illness. Consideration should be given to the availability of e-signature facilities. If a trustee will be absent for a prolonged period then consider the use of powers of attorney.
Member communications	Consider an announcement to members or Q&A covering likely member enquiries. Specific messaging may be needed for members close to retirement and advice on this communication should be sought first. Additional information may be needed to accompany DC benefit statements where fund values may have decreased dramatically. The Money and Pensions Service (MaPS) has produced guidance that includes protective steps that savers can take now to avoid money worries later on, and includes a section entitled *If you're worried about your pension*[10].
Integrated Risk Management (IRM)	• Trustees should, with their advisers, consider the potential impact on employer covenant, scheme investments and funding. Employer covenant may need regular monitoring throughout the crisis. • Employers have a duty to disclose information that is of material significance in the exercise by the trustees of any of their functions. Trustees and employers have a duty to report 'notifiable events' to TPR. • Where material changes make it unsafe to continue to rely on the chosen assumptions used in funding and investment documents, trustees should review and, if necessary, revise those documents. It is not always necessary to commission an out-of-cycle valuation to do this. • Sponsors may seek relief from / deferral of deficit recovery contributions. The starting point for DB pension schemes is the IRM framework.

10 https://www.moneyadviceservice.org.uk/en/articles/coronavirus-and-your-money

DC and ancillary benefits	An integrated risk management approach works for DC schemes too, although the focus would be more around contributions, investments and governance: • Ensuring contributions continue to be paid in accordance with payment schedules and automatic enrolment (AE) requirements for AE schemes. • Monitoring of default funds (where most members are usually invested). • Reviewing DC investment options, particularly default funds. Consideration also needs to be given to ancillary benefits such as life cover. Policies may need to be reviewed to check for provisions that may cap the number or value of claims. Rules need to be reviewed to see if there are potential uninsured liabilities.
Transfers	For DB schemes, should transfer value (TV) basis be reviewed? Should transfers be suspended? For DC members, transfer pro-formas may need updated to alert members about market volatility and the risk of large discrepancies between TVs quoted and TVs actually paid.
Risk transfer and member option exercises	Planned buy-ins and buy-outs should be reviewed, as should member option exercises such as 'ETVs', 'PIE' and 'trivial pension commutations'. Advice should be sought on any plans to increase hedging.

***John Wilson**, Head of Technical, Research and Policy,*
Dalriada Trustees

Dalriada. A better way

Dalriada Trustees Limited is a privately owned professional and independent trustee and has operated since 2003.

Dalriada can act as an independent trustee to any size of pension scheme from those operated by small private companies to large schemes associated with major listed public companies.

Our team includes both highly experienced DB independent trustees and specialist DC independent trustees who can both serve on trust based boards (including acting as a non-affiliated trustee of a Master Trust) or act as members of governance committees (including Internal Governance Committees operated by providers).

The Pensions Management Institute would like to thank its Insight Partners and other supporters for their continued contribution to the Institute at this difficult time. Their dedication - as evidenced by the outstanding content in this report – plays a pivotal role in ensuring that the PMI is able to continue to operate in the midst of the COVID-19 difficulties. We have a dedicated central staff who have been able to continue working from home since the commencement of lockdown, but the input of individual volunteers and corporate sponsors remains essential. We would like to offer them our sincere thanks.