Financial Management Plan: Interim monitoring of the 2020 valuation

Executive Summary

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Outcome: NOTING
Meeting: Joint Negotiating Committee ("Committee"), 29 March 2022
Annex: A: 2020 valuation interim monitoring report: February 2022

Purpose:

To provide the Committee with the 2020 valuation interim monitoring report in respect of the Scheme as at 28 February 2022.

Outcome:

The Committee is invited to **NOTE** the development of the Scheme under the interim monitoring of the 2020 valuation.

Questions and Conclusions:

1. What do the updated monitoring figures show?

- Since the valuation date, the indicative Technical Provisions deficit has fallen due to the increase in asset prices being greater than the increase in Technical Provisions liability. The indicative self-sufficiency deficit is also lower than on the valuation date which translates into an improved risk position.
- The indicative future service contribution requirement is slightly higher than on the valuation date; however, required deficit recovery contributions have decreased leading to an indicative lower total contribution than at the valuation date.
- During February, the modelled technical provisions and self-sufficiency deficits fell due to rising gilt yields decreasing the value of liabilities, which outweighed the £0.5bn fall in the asset value.
- Inflation expectations are significantly higher than at the valuation date, leading to the cost saving resulting from the 2.5% inflation cap on the new benefit structure increasing since the valuation date. The higher inflation expectations mean that removing this cap for the new benefit structure would lead to a significant increase in contribution requirements. The figures make approximate allowance for the delay to the implementation of the new pension increase cap.
- If a similar position to that indicated by the monitoring was established at the next valuation, it may be possible to reduce contributions or increase benefits or some combination of both.
- The amber rating on the affordable risk capacity indicates the strength of technical provisions is still a watch item.

- The volatility in many of the key inputs over recent months indicates significant care should be taken in reaching any conclusions. Since the end of February, we have seen considerable volatility in the markets

Why is the JNC receiving this paper:

To give the JNC an update on the Trustee's development of its monitoring of the 2020 valuation and to provide an update of what the interim monitoring is showing.

Input received from other boards / committees and other parts of the business/external advisers:

The paper contains various data provided by USSIM and the Scheme Actuary, in particular expected long-term returns and/or discount rates on the various portfolios, the discount rates used to determine the ARC values. The asset value has been provided by USSIM.

Paper status justification:

Unrestricted. A version of Annex A is published on the USS website https://www.uss.co.uk/about-us/valuation-and-funding/our-valuations.

Any actuarial information referred to in this paper was created for the Board of USSL only, including in preparing its response, and may not be relied upon by any other party. This paper is provided only to inform the JNC of matters considered by the Board. The data and information in this paper are not intended to contribute in whole or in part to any decisions made by the JNC. If it or any other party believes actuarial advice on which it may place formal reliance is required to assist its decisions on these matters, it should obtain its own advice.

Annex A: 2020 Valuation Interim Monitoring Report Summary

Summary

The Committee is invited to **NOTE:**
- The interim monitoring report in the annex, and the summary below.

What do the updated figures based on the 2020 valuation interim monitoring approach show?

Based on the 2020 valuation monitoring methodology, as at 28 February 2022:
- Assets have significantly increased from £66.5bn on the 31 March 2020 valuation date to £88.8bn (although they have fallen during 2022).
- There has been a fall in USSIM's long-term return expectations, which has reduced the discount rates and increased liabilities since the valuation date.
- The net effect of the above two points is to reduce the indicative technical provisions deficit from £14.1bn on the valuation date to £2.0bn at the end of February.
- The indicative future service cost is slightly higher than at the valuation date, however the lower deficit would reduce deficit recovery contributions, leading to an overall lower contribution requirement. The RAG status of each contribution metric is Green.
- The indicative self-sufficiency deficit has also decreased during February to stand lower than on the valuation date.
- The RAG status of the IRMM metric (self-sufficiency deficit as percentage of affordable risk capacity) remains Amber, as it was at the end of January, albeit now closer to the Green threshold.
- Metrics A, B and C have the same status as at the end of January (Amber, Amber and Green respectively).

Calculation basis

Note that the figures in the attached report have been estimated based on an interim approach to monitoring the 2020 valuation. The pre-retirement discount rates used are the same as at 31 December 2021, as updated FBB expected returns have not been produced for 28 February 2022. The figures have not been updated for the additional liabilities relating to late retirements and cash transfer sums described in the Scheme Actuary's June 2021 advice, but the contribution rates have been approximately adjusted to allow for the agreed delayed implementation of the 2.5% pa pension increase cap.

FMP Monitoring - End February 2022
For JNC information
Benefit changes from 1 April 2022

Assets	**31-Mar-20**	**28-Feb-22**
Assets	£66.5bn	£88.8bn

Technical Provisions	**31-Mar-20**	**28-Feb-22**
Deficit	£14.1bn	£2.0bn
Liability	£80.6bn	£90.8bn
FBB Pre ret 30 yr expected return	Gilts + 5.28%	Gilts + 3.72%
Pre-retirement discount rate	Gilts + 2.75%	Gilts + 2.45%
Post-retirement discount rate	Gilts + 1%	Gilts + 0.60%
Gilts (single equivalent) nominal	0.7%	1.5%
CPI (single equivalent)	2.1%	2.8%
CPI with 2.5% cap (single equivalent)	1.7%	2.1%
Single equivalent discount rate	Gilts + 1.6%	Gilts + 1.3%
	CPI + 0.3%	CPI + 0.0%
'Breakeven' discount rate		Gilts + 1.36%
in respect of TP liabilities		CPI + 0.02%

Self-Sufficiency	**31-Mar-20**	**28-Feb-22**
Deficit	£35.5bn	£27.7bn
Liability	£102.0bn	£116.5bn
Discount rate	Gilts + 1%	Gilts + 0.60%
Gilts (single equivalent) nominal	0.7%	1.5%
CPI (single equivalent)	2.6%	3.3%
Single equivalent discount rate	CPI - 0.9%	CPI - 1.2%

Note: Figures on the valuation date include an allowance of £0.5bn liabilities and 0.4% DRC for certain late retirement entitlements and short service members with less than two years' service who retain rights to cash transfer sums. This allowance is not included in subsequent monitoring figures. The FBB expected returns shown exclude effects of rebalancing. The 'Breakeven' discount rate is that at which the TP liability value equals the asset value.

FMP Monitoring - End February 2022
For JNC information
Benefit changes from 1 April 2022

Future Service Cost	31-Mar-20	28-Feb-22
Future Service Cost	25.2% *	25.6%
Ratio FSC to amount being paid		102%
RAG status		Green

Deficit Recovery Contribution	31-Mar-20	28-Feb-22
Remaining recovery period and 0.25% outperformance	6.2% *	0.0%
10 year recovery period and no outperformance		2.0%
RAG status		Green

Total Contribution	31-Mar-20	28-Feb-22
Remaining recovery period and 0.25% outperformance	31.4% *	25.6%
10 year recovery period and no outperformance		27.6%
RAG status		Green

* Amount calculated as at the valuation date; Deficit Recovery Contribution based on 0.5% outperformance.

Allowance is made for an element of additional investment returns of 0.5% pa for 18 years within the FSC on the valuation date but not at subsequent dates. The DRC calculation is approximate and assumes an immediate change in contributions. The FSC has been adjusted approximately for the agreed delayed implementation of the 2.5% pa pension increase cap allowing for changes in market conditions.

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For JNC information
Benefit changes from 1 April 2022

Affordable Risk Capacity (ARC)	31-Mar-20	28-Feb-22
Affordable Risk Capacity	£30 - 33bn	£32 - 35bn
IRMM (Self-suff deficit as % of ARC)	113%	83%
RAG status		Amber
ARC discount rate	Gilts + 1.2%	Gilts + 0.95%

Metrics	31-Mar-20	28-Feb-22
Metric A	10.0	7.5
Metric A - RAG status	Green	Amber
Metric B	-4.0	5.5
Metric B - RAG status	Red	Amber
Metric C	40.6	48.4
Metric C - RAG status	Green	Green

Covenant	31-Mar-20	28-Feb-22
Covenant	Strong	Strong
RAG status		Green

This report should be read in conjunction with the notes in the covering paper. The figures in this report have been derived for the purpose of monitoring the movement in funding over time. The approach adopted is not as accurate as when determining the liabilities in a one-off calculation and therefore these figures are not intended to be used as a basis for advice without further consideration. This report is provided for information only.

FMP Monitoring - End February 2022
For JNC information
APPENDIX A - RAG rating definitions

IRMM

Self-sufficiency deficit as percentage of affordable risk capacity

Green	Less than 80%
Amber	Between 80% and 115%
Red	Greater than 115%

Future Service Cost

Ratio of future service cost to future service contribution being paid

Green	Up to 115% (c28% based on proposed post 1 April 2022 benefits)
Amber	115% to 125% (c28%-31%)
Red	Above 125% (c31%)

Deficit Recovery Contribution

1) Deficit contribution requirement over the remaining recovery period allowing for outperformance (0.25%pa from 2021 Scheme Actuary review)
2) Deficit contribution requirement over a ten year recovery period with no allowance for outperformance

Green	If actual DRC payable is at least those required under both calculations 1 and 2 above
Amber	If the actual DRC payable is lower than that under calculation 1 or 2
Red	If the actual DRC payable is lower than that under both calculations 1 and 2

Total contribution

Green	If the total contribution requirement using DRC calculations 1 and 2 above is less than or equal to the total contribution being paid
Amber	If the total contribution requirement using DRC calculation 1 or 2 above is less than or equal to the total contribution being paid
Red	If the total contribution requirement using DRC calculations 1 and 2 above is greater than the total contribution being paid

Covenant

Green	“Strong”, as assessed by the covenant advisor
Amber	“Strong” but on negative watch
Red	“Tending to Strong” or lower

FMP Monitoring - End February 2022

For JNC information

APPENDIX B - Metric definitions

Metric A

Affordable risk capacity less (self-sufficiency liability less TP liability)

Green	Headroom > Asset transition and demographic risks
Amber	Asset transition risk < Headroom < Asset transition risk and demographic risks
Red	Headroom < Asset transition risk

Metric B

Affordable risk capacity less self-sufficiency deficit

Green	Headroom > Asset transition risk
Amber	0 < Headroom < Asset transition risk
Red	Headroom < 0

Metric C

Available risk capacity less self-sufficiency deficit

Green	Headroom > ‘Value at risk’
Amber	Asset transition risk and demographic risk < Headroom < ‘Value at risk’
Red	Headroom < Asset transition risk and demographic risk

Note

Asset and demographic transition risk, and available risk capacity, have not been updated since the valuation date

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APPENDIX C - Benefit changes not enacted

Technical Provisions	31-Mar-20	28-Feb-22
Deficit	£18.4bn	£6.3bn
Pre-retirement discount rate	Gilts + 2%	Gilts + 1.8%
Post-retirement discount rate	Gilts + 1%	Gilts + 0.60%

Future Service Cost	31-Mar-20	28-Feb-22
Future Service Cost	37.0%	40.7%
Ratio FSC to amount being paid		163%
Amount being paid	24.9%	

Deficit Recovery Contribution	31-Mar-20	28-Feb-22
Remaining recovery period and 0.25% outperformance	15.6% *	4.0%
10 year recovery period and no outperformance		6.2%
Amount being paid	6.3%	

Total Contribution	31-Mar-20	28-Feb-22
Remaining recovery period and 0.25% outperformance	52.6% *	44.7%
10 year recovery period and no outperformance		46.9%
Amount being paid	31.2%	

* Equivalent Deficit Recovery Contribution calculated on the valuation date based on 0.5% outperformance for the first 10 years.