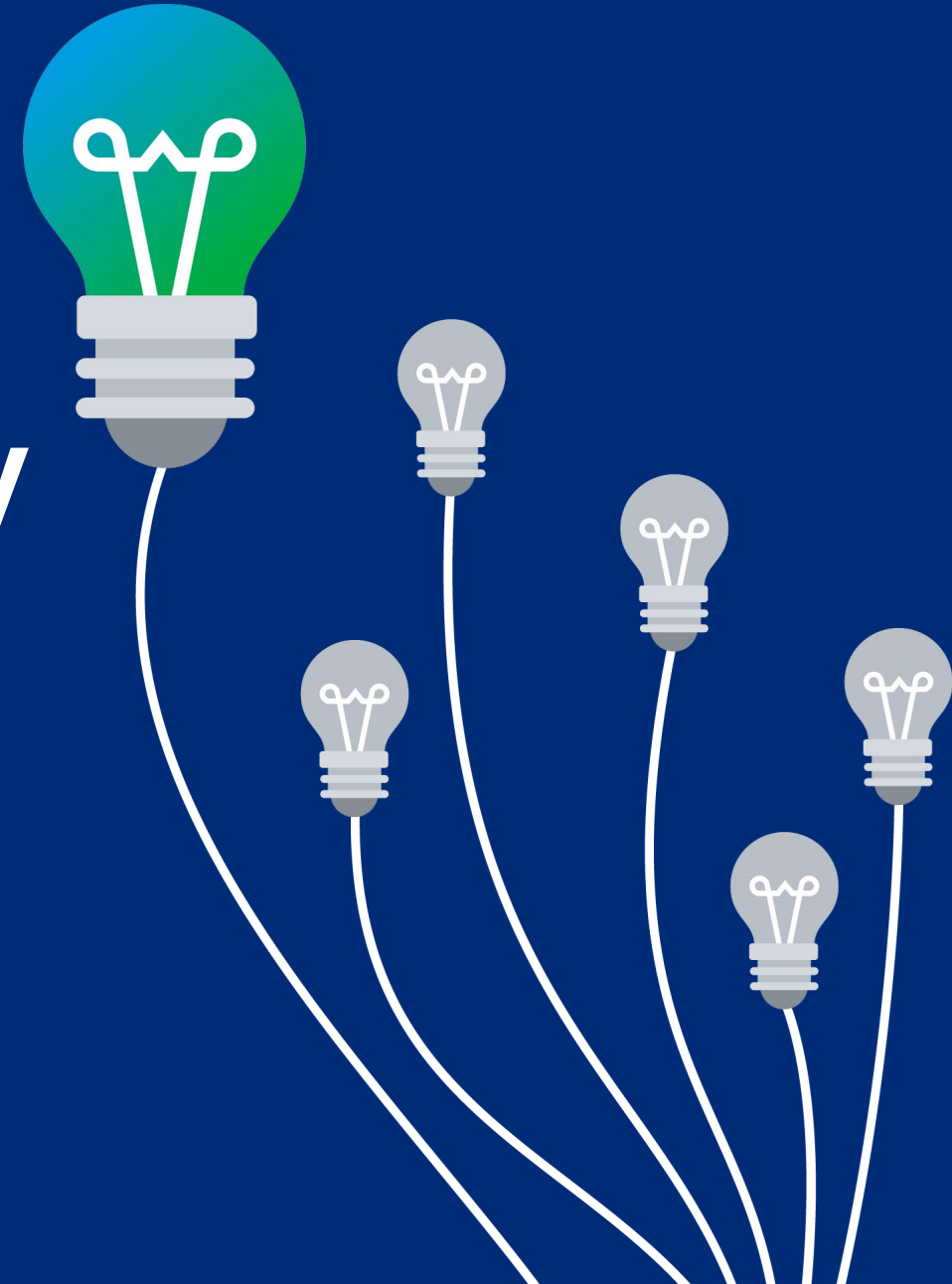


# Learnings about the objectives and resiliency of pension systems



29 April 2022

Dr David Knox, Senior Partner

# Lessons from COVID and beyond



Objectives or Purposes  
of Retirement Systems



Resiliency of Pension  
Schemes



Some Conclusions for the  
Future



# Agenda

# Learnings about the objectives and resiliency of pension systems

## What are the objectives of a retirement system?

To alleviate poverty for the old



To enable most retirees to maintain their “previous” standard of living

## Two Objectives mean at least Two Systems

Public pension

Funded pension arrangements (income smoothing over a lifetime)

These broad objectives must have a long term focus

Clear objectives help the alignment of all stakeholders

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## What are the objectives of a retirement system?

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Funded pension arrangements (income smoothing over a lifetime)

**Multi pillar systems reduce risks and broaden opportunities**

**These broad objectives must have a long term focus**

**Clear objectives help the alignment of all stakeholders**

# **Lessons learned relating to delivering the objectives**



# Global trends affecting retirement outcomes

Changes in the Mercer CFA Institute Global Pension Index

## 2020 to 2021 (39 systems)



Household savings increased

**+>3% of income**

On Average

**+>8%**

Canada, New Zealand, Australia, UK



Government debt increased in an era of historic low interest rates

**+>4% of GDP**

On Average

**+>10%**

India, Hong Kong, Norway



Pension fund assets increased

**+>4% of GDP**

On average

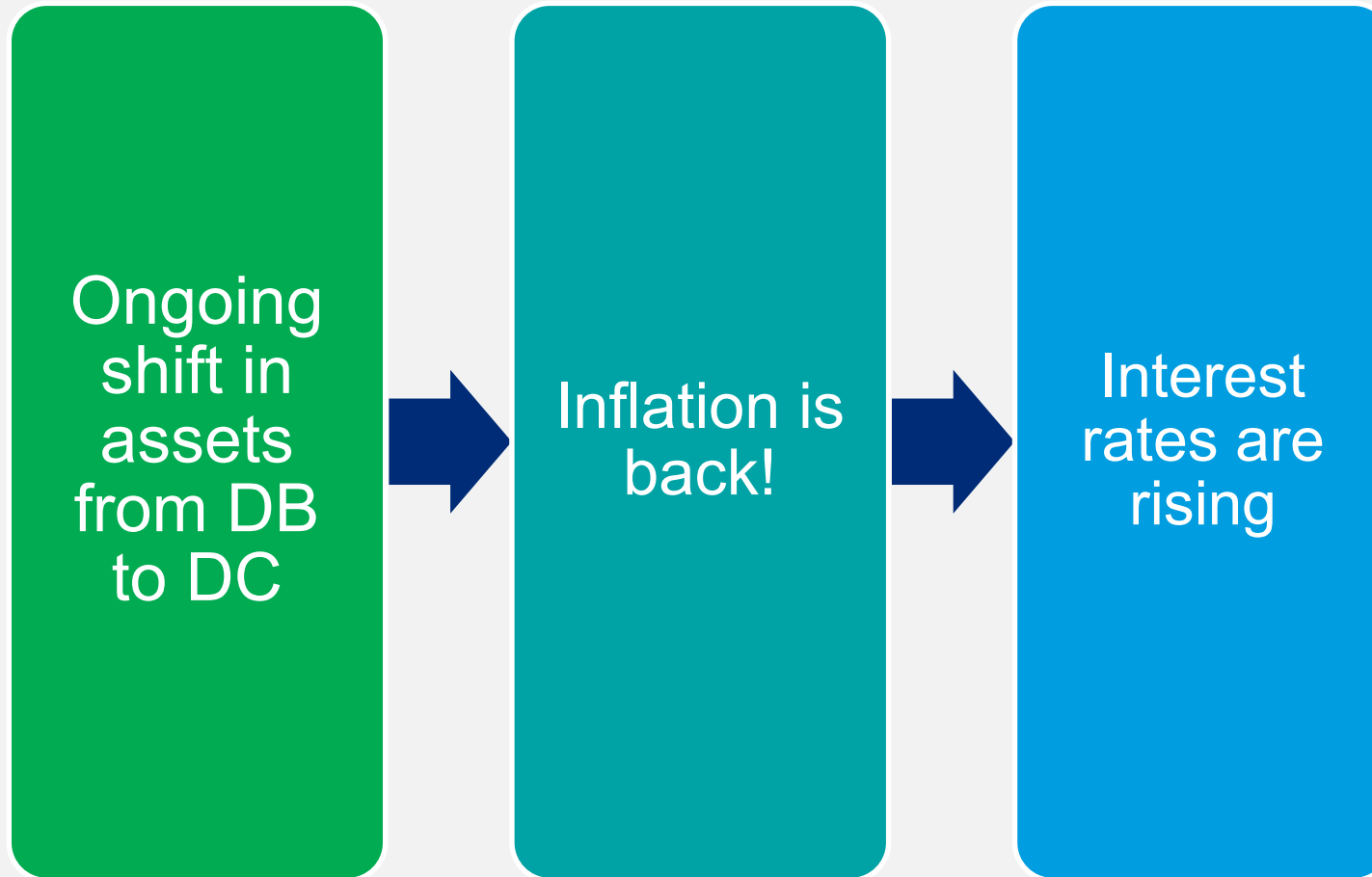
**+ 6.9% pa (1yr)**

**+ 6.8% pa (10 & 20 yrs)\***

All pension systems to end 2021

\*Source WTW

# Global trends affecting retirement outcomes



**Lesson:**  
The world is changing.

We need to think beyond traditional paradigms



# Event: Early release of assets

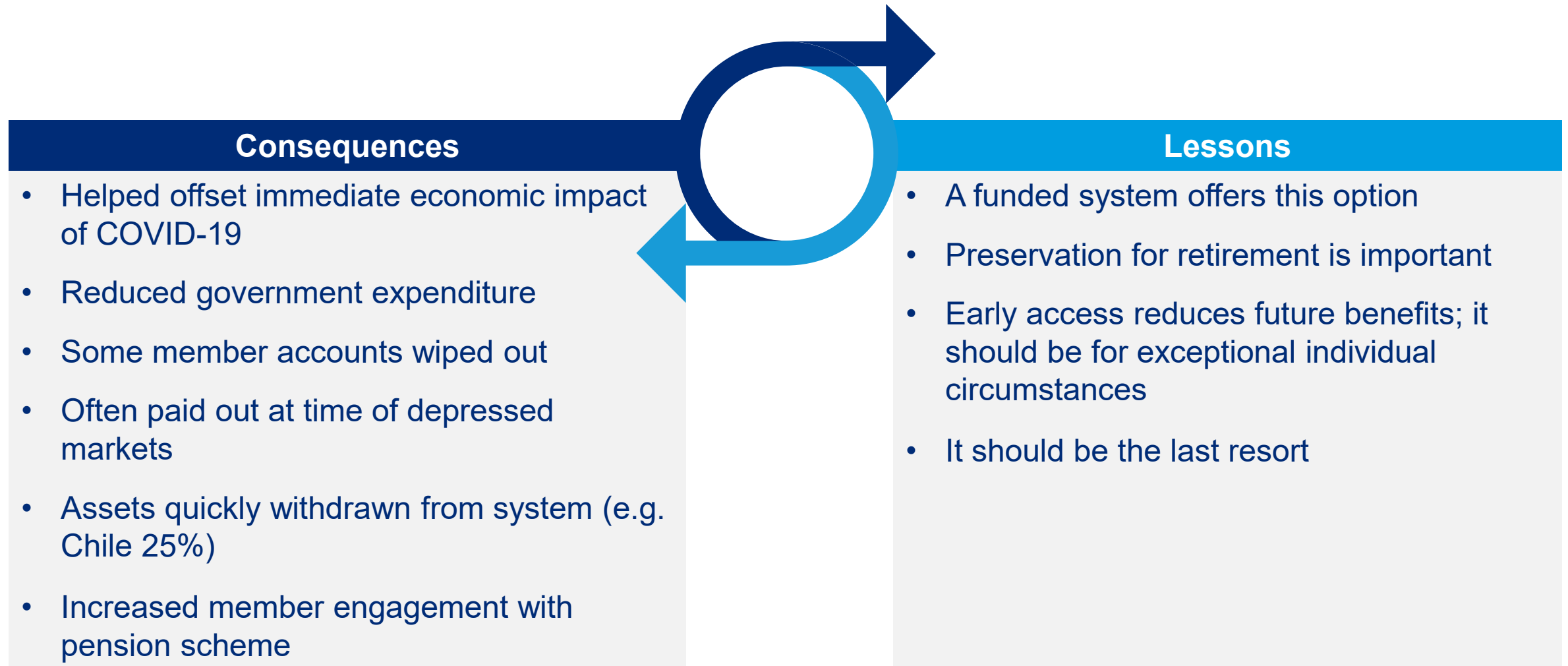
## Consequences

- Helped offset immediate economic impact of COVID-19
- Reduced government expenditure
- Some member accounts wiped out
- Often paid out at time of depressed markets
- Assets quickly withdrawn from system (e.g. Chile 25%)
- Increased member engagement with pension scheme

## Lessons



# Event: Early release of assets



# Result: COVID-19 adds to inequality

Early release of benefits has long term consequences

Some industries were more affected than others e.g. hospitality, tourism

Greater impact on low income earners and women

Government financial support for the affected normally excluded pension contributions

Pension gaps were widened

# Result: COVID-19 adds to inequality

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## Lessons:

- Financial support should include pension contributions (Netherlands and UK)
- We need to develop measures to reduce gender pension gap (e.g. pension baby bonus for primary carers)
- Review interaction between public and private pensions over the long term

# Question:

*Can pension outcomes  
be maintained?*

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## Facts

- Reduced pension contributions for many
- Reduced company support in voluntary arrangements
- Reduced workforce opportunities for some
- Reduced investment returns for a period
- Work life balance has become more important

## Options for individuals

- Take more investment risk
- Review likely retirement age
- Review retirement expectations
- Review pension contributions

## Fact: Mortality rates have been affected

- Increased mortality in some age groups and some cohorts
  - The impact has not been universal
  - Skewed towards lower income groups
- Most DB funds have had less impact
- Long term COVID-19 effects remain unclear

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## Lessons

- Life expectancy gap between socio-economic groups likely to widen
- Consequences for pension design (e.g. pooling) and compulsory/default arrangements in retirement

# Investment choice by individual members

- Common in DC arrangements to enable individuals to switch portfolios
- A flight to safety often occurs in a market downturn or increased uncertainty
- Older members are more likely to switch, possibly too late
- Many do not switch back and miss out on the recovery



## Lessons

1. Long term perspective is key
2. Information and advice are helpful
3. Is member choice and freedom always a good idea?

# A case study – Aware Super

Assets \$A130 billion | >1 million members | many in the NSW public sector a DC plan

Between 3 Feb and 6 April 2020	Total membership	> 55 without advisor	> 55 with advisor
% membership who switched	2.7%	7.7%	1.8%
% defensive switches	79%	75%	81%
% into cash	46%	43%	54%
% of total FUM switched		11%	1%
Average % of balance switched		84%	33%



By August 2020, two-thirds who had switched to cash **were still in cash.**

**Lesson:**  
DC plans need to be prepared for similar future outcomes to the detriment of their members' benefits



# Question: What level of individual responsibility is best?

## Global trend

DB pension schemes with corporate sponsors to DC schemes with individual responsibility

- Risk transfers relating to investment returns; salary movement; expenses; inflation; longevity

## COVID-19 and other consequences

- Increased government debt which places future public pensions at risk
- Risk averse corporates reducing pension commitment
- Changing labour markets with reduced long term commitment and reduced coverage
- Growing pension assets and household savings for some!



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## Lessons:

- There is a need to protect and provide for all pension consumers with appropriate defaults through accumulation and pension phases
- Increased pension coverage is needed so all workers have pension accounts
- The balance between individual responsibility and risk pooling needs to be developed
- Broaden the discussion to include all pillars

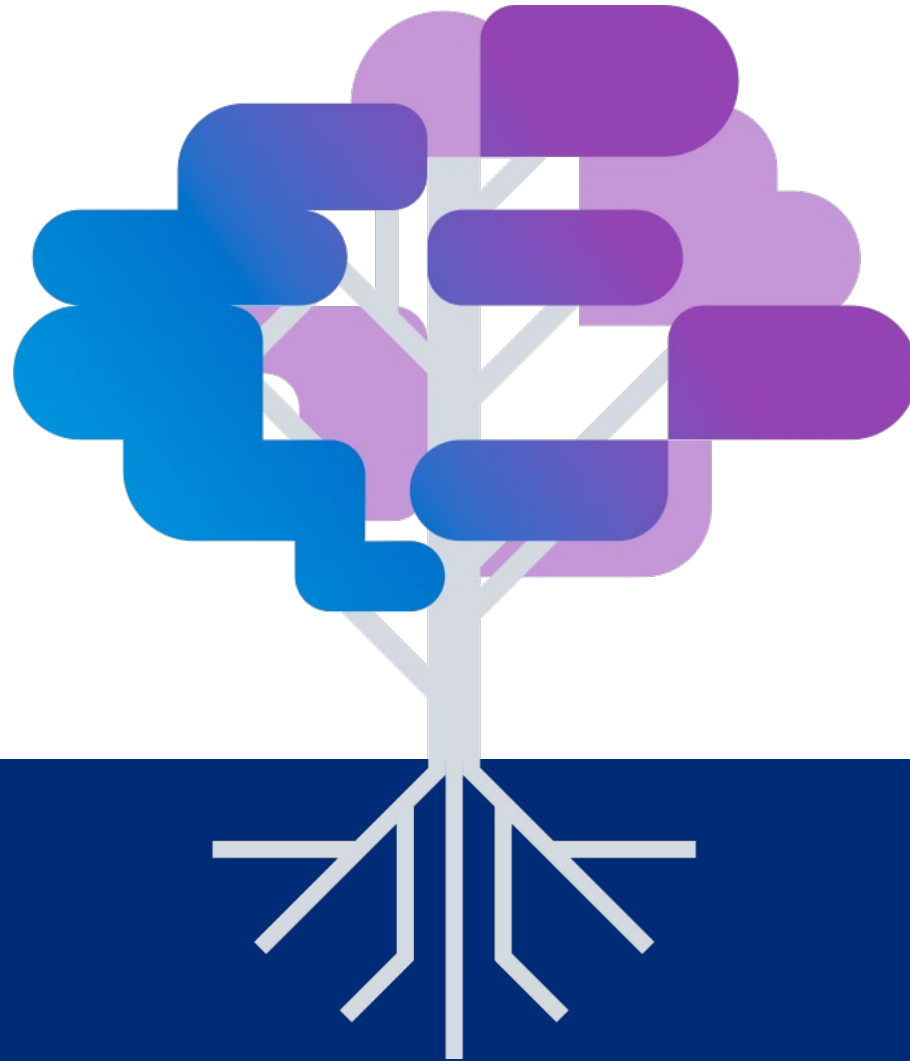
# Lessons learned relating to the resilience of pension schemes



# What is resilience?

**Resilience is the capacity to recover quickly from difficulties**

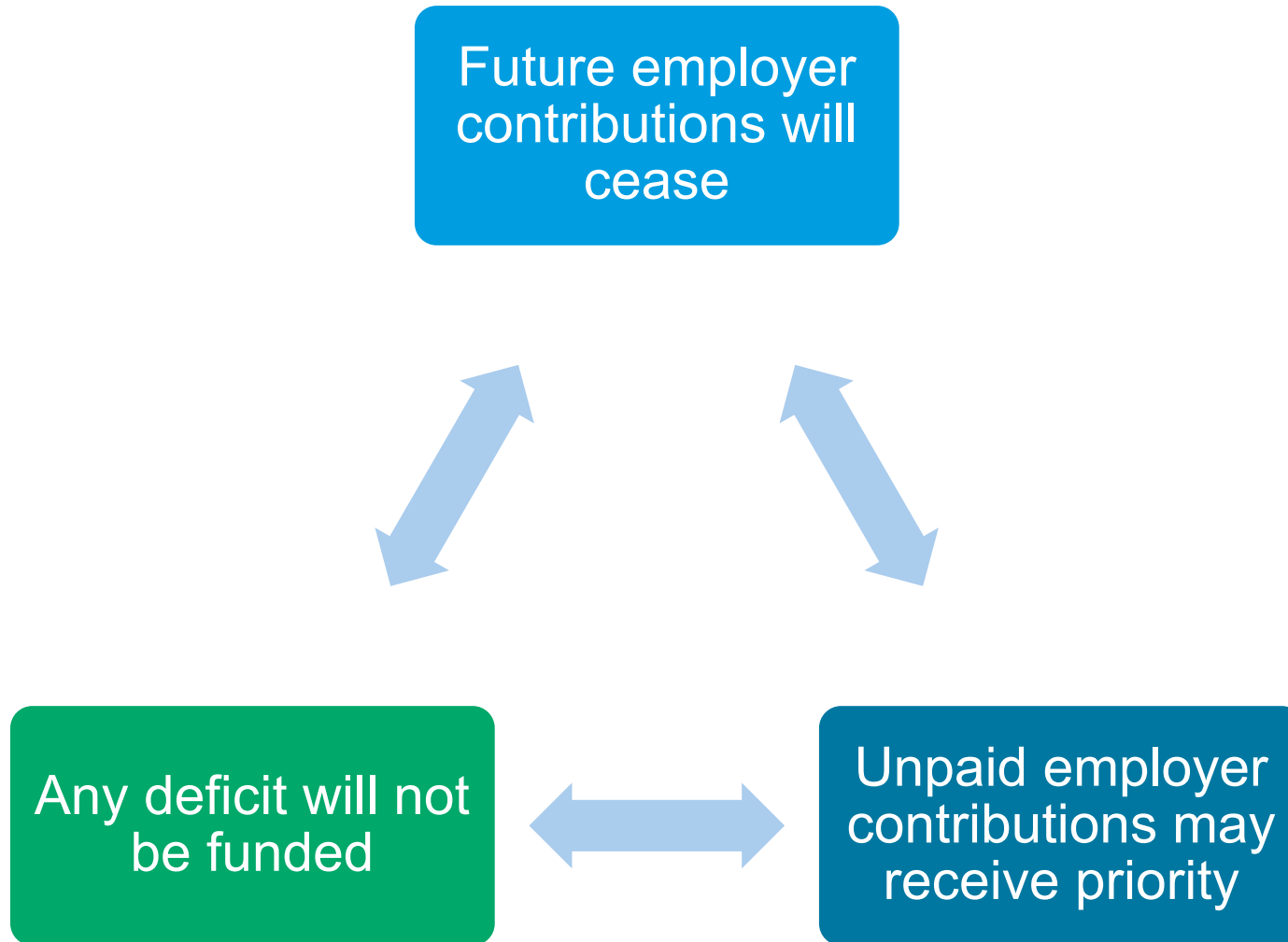
Clearly resilience of pension schemes is important for the retirement system to deliver on its objectives



But ... What are the risks or events that might affect this resilience?

# Event: Corporate failure

COVID-19 has led to some corporate failures



## Lessons!

Funding status, based on realistic assumptions, is important

Pension funds should not rely on the corporate sponsor

Good times in the future cannot be guaranteed – there are risks!

# Event: Poor investment return

Is it industry wide (i.e. systemic) or pension scheme specific?

Is it short term or longer term?

What are the causes?

Most markets will bounce back over the long term but ...

What is the regulator's response?

The pension scheme's brand may be damaged

## Lessons!



Don't get isolated – that's a risk

Robust plans needed for unforeseen events

Communicate and explain – build trust

# Event: Liquidity is stretched

## Significant benefit payments are a risk

There are many possible causes – e.g. corporate restructure, aging membership, government decision, media story, member switching

## It's important for schemes to undergo stress testing

Where are the pressure points?

Are assets marketable?

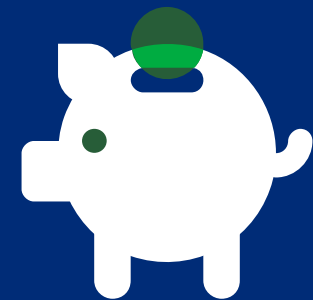
# Event: Liquidity is stretched



## Lessons!

Pension schemes are resilient but planning is important

The unexpected does occur – be ready!



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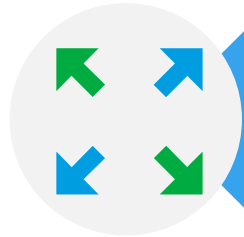


# Event: Poor operations



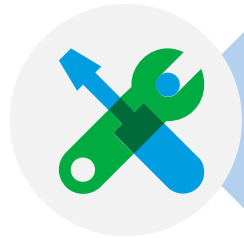
The consequences of poor service can escalate through social media

- Communication is important



How much control does the pension scheme have over outsourced arrangements?

- What are the expectations?



Insourced arrangements may be harder to fix quickly



How will members respond to faults?



## Lessons!

Develop a culture - learn from near misses or shortcomings

There needs to be constant monitoring

Be agile as conditions change e.g. government announcements

# Event: Political and regulatory intrusion

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## Lessons!



Keep telling the story!  
What is the purpose?

Be proactive and fix the problems. Don't wait for government!

Anticipate the issues

Understand the role and purpose of the regulators

# Conclusions



# The future retirement system

## Alleviate poverty amongst the aged

Public pensions will  
continue to be important  
but:

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## Increase individual responsibility

- This has many positives but some negatives too
- They will need more help, guidance and advice
- This will extend beyond the private pension sector

# THANK YOU

