

# Press Release

## UK FINAL SALARY PENSION SCHEMES: MOST SCHEMES DANGEROUSLY UNDERHEDGED AGAINST INFLATION

London, 14 December 2011

In light of persistent inflation and recent statutory changes, Redington and Pension Corporation conducted a survey of actuaries and trustees on the impact of the switch in indexation from RPI to CPI on their schemes. Participants of the survey are responsible for defined benefit liabilities and the following paper discusses their views of the industry and the future.

### Key findings:

- Fewer than 20% of defined benefit pension schemes have at least 50% of their inflation-linked pensions backed with inflation-linked assets such as index-linked gilts.
- 64% of actuaries said that schemes they advised would “likely” or “almost certainly” carry out a buy-out or buy-in over the next three years while 39% of trustees believed in this outcome.
- 91% of trustees said they would “likely or almost certainly” consider better asset liability matching over the same period.
- The overwhelming majority of schemes are structurally underhedged for inflation and therefore are highly vulnerable to future inflation increases
- Newly announced infrastructure projects may provide a further source of inflation hedging
- The BoE predicts that inflation will fall sharply over the next year, with CPI forecast to decline below 2% by the end of 2012. Counterintuitively, the CPI/RPI spread could become *more* pertinent to many schemes in the context of waning inflation
- This general inflation risk poses a much greater risk to most schemes than CPI/RPI basis risk and the priority of these schemes should be to increase overall levels of inflation protection

Commenting on the results, Robert Gardner of Redington said: “The switch in statutory indexation from RPI to CPI has impacted schemes looking to de-risk. Taking stock of their current stand point, pension schemes can do a significant amount of first order inflation de-risking using RPI before they need to worry about second order RPI/CPI basis risk”.

Jay Shah of Pension Corporation added: "Pension schemes are continuing to take a big risk of inflation eroding away investment returns, and funding positions subsequently deteriorating. So whilst it is good news that de-risking is now at the top of the agenda for trustees, they should consider hedging inflation a core part of this process., Trustees should look at how they can best remove risk from their scheme in whatever form, even if they aren't able to insure, given current funding levels."

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For more information, please contact:

Gurjit Dehl, Redington: [gurjit.dehl@redington.co.uk](mailto:gurjit.dehl@redington.co.uk)  
020 3326 7102 / 07974 645 462

Jeremy Apfel, Pension Corporation [Apfel@pensioncorporation.com](mailto:Apfel@pensioncorporation.com)  
020 7105 2140

## Notes to editors:

### About Redington

Founded in 2006, Redington was established by two investment bankers, Dawid Konotey-Ahulu and Robert Gardner, formerly of Merrill Lynch, offers asset and liability management to pension funds and insurance companies. The company employs 45 people and has over £200bn in asset under consulting.

Konotey-Ahulu and Gardner spent several years advising on risk management strategies for their clients and, in 2003, devised and implemented the first full LDI risk management transaction by a pension fund, Friends Provident Pension Scheme. Their experience allows them to harness effectively the technology of investment banks and asset managers to provide clients with a wide range of solutions.

Redington is an advocate of social media and web 3.0 and how it can be used to bring about innovation and collaboration in the pensions community. In December 2009 it launched mallowstreet.com, a targeted community that brings pension fund decision makers and product providers together.

[www.redington.co.uk](http://www.redington.co.uk)



### About Pension Corporation

Pension Corporation is a leading provider of risk management solutions to the trustees and sponsors of defined benefit pension funds. Its FSA authorised and regulated insurance company, Pension Insurance Corporation ("PIC"), brings safety and security to scheme members' benefits through innovative, tailored solutions factored around pension insurance buyouts and pension insurance buy-ins. PIC has c.£4.5bn in assets and has insured more than 50,000 pension fund members. Clients include FTSE 100 companies, multinationals and the public sector. PIC concluded the first UK public sector backed pension insurance buyout and the first buyout over £1 billion. PIC is proud to work with pension fund trustees to maximise member benefits.

For further information please visit [www.pensioncorporation.com](http://www.pensioncorporation.com)