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Merchant Navy Officers Pension Fund

**Annual funding update
as at 31 March 2008**

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30 October 2008

Background

- An annual funding update is required under the Pensions Act 2004 in the years in which a full actuarial valuation is not undertaken.
- This is not a full actuarial valuation, but a roll forward of the 31 March 2006 valuation results, taking into account actual cashflows. The asset value as at 31 March 2008 has been taken from the Fund's Annual Report.
- The same methodology as that used for the 2006 valuation has been used to derive the financial assumptions, but based on 31 March 2008 market conditions. It is a requirement to follow the methodology adopted for the most recent full actuarial valuation. No adjustment has been made for any change in the strength of the employers' covenant.
- The statistical (or demographic assumptions) used are the 2006 assumptions. They will be reviewed at the next formal valuation in 2009, with particular focus on the mortality assumptions (especially future rates of improvement for the New Section).
- Over the two years to 31 March 2008, long dated yields fell by 0.4% pa for index linked, whereas fixed interest gilt yields rose by 0.1% pa. Corporate bond yields have risen by 2.0% and this increased margin between gilts and corporate bonds has been partially reflected in the discount rates. Expectations of long term inflation also rose by about 0.75% pa.
- The funding position is subject to considerable volatility, and can change significantly from month to month. Thus the current position could be materially different from that disclosed as at 31 March 2008.

Changes to financial assumptions

Ongoing Basis – Old Section

	31 March 2006	31 March 2008
Price inflation	3.00%	3.75%
Investment return:		
- pre retirement	4.50%	5.00%
- post retirement	4.50%	5.00%
Pension increases	0.00%	0.00%

Ongoing Valuation Results

Results on ongoing basis – Old Section

	31 March 2006 (£m)	31 March 2008* (£m)
Liabilities in respect of benefits accrued to date	1,351	1,275
Reserve for expenses	25	25
Total Liabilities	1,376	1,300
Assets	1,473	1,295
Surplus	97	(5)
Funding Level	107%	100%

*The 31 March 2008 results allow for the 4% bonus which was awarded by the Trustee as at 1 April 2007.

The ongoing surplus has reduced by about £102m over the two years to 31 March 2008 as a result of:

- Change in market conditions reducing the value of liabilities (+£70m)
- Investment returns and other miscellaneous items (-£121m)
- 4% bonus awarded as at 1 April 2007 (£-51m)

Discontinuance Results

Old Section

Discontinuance Results – Old Section

	31 March 2006 (£m)	31 March 2008* (£m)
Liabilities in respect of benefits accrued to date	1,436	1,420
Reserve for expenses	35	35
Total Liabilities	1,471	1,455
Assets	1,473	1,295
Surplus/(Deficit)	2	(160)
Funding Level	100%	89%

*The 31 March 2008 results allow for the 4% bonus which was awarded by the Trustee as at 1 April 2007.

The discontinuance funding level has deteriorated because the reduction in the value of assets held has not been offset by the change in the value of liabilities, which under this basis is linked directly to the yields on gilts.

It should be noted that this is only an estimate of the buy-out cost for the purposes of GN9. The true position can only be determined by completing a buy-out. The Old Section is in receipt of recent quotes which indicate that the Section is likely to have sufficient assets to cover its liabilities in full.

Changes to financial assumptions

Ongoing Basis – New Section

	31 March 2006	31 March 2008
Price inflation	3.00%	3.75%
Investment return:		
- pre retirement	7.00%	7.20%
- post-retirement	4.75%	5.00%
Salary increases	4.50%	5.25%
Pension increases		
- pre 97	0.00%	0.00%
- post 97	3.00%	3.75%

Ongoing Valuation Results

New Section

Results on ongoing basis – New Section

	31 March 2006 (£m)	31 March 2008 (£m)
Liabilities in respect of benefits accrued to date	2,047	2,047
Reserve for expenses	35	35
Total Liabilities	2,082	2,082
Assets	1,931	1,999
Surplus/(Deficit)	(151)	(83)
Funding Level	93%	96%

The ongoing deficit has reduced by about £68m as a result of:

- 2006 deficit contributions, plus interest, recognised in the accounts: +£169m
- Change in market conditions reducing the value of liabilities: +£47m
- Investment returns and other miscellaneous items: -£148m

The results of this update indicate that a further deficit of £83m has emerged over the two years since 31 March 2006.

Discontinuance Results

New Section

Discontinuance Results – New Section

	31 March 2006 (£m)	31 March 2008 (£m)
Liabilities in respect of benefits accrued to date	2,831	2,910
Reserve for expenses	50	50
Total Liabilities	2,881	2,960
Assets	1,931	1,999
Surplus/(Deficit)	(950)	(961)
Funding Level	67%	68%

The discontinuance funding level has deteriorated because the reduction in the value of assets held has not been offset by the change in the value of liabilities, which under this basis is linked directly to the yields on gilts.

It should be noted that this is only an estimate of the buy-out cost for the purposes of GN9. The true position can only be determined by completing a buy-out and recent experience indicates that better quotes could be obtainable.

Regulator's consultation on assumptions (mortality) – February 2008

- The Pensions Regulator has issued a consultation document on mortality assumptions.
- “There are two separate decisions for trustees on mortality assumptions:
 - the baseline table for the current rates of mortality; and
 - the allowance for future improvements.”
- The Regulator indicated guidance on each of these.
- The Trustees will need to consider mortality for the 2009 valuations in the light of the Regulator's final guidance.
- Following the initial guidance, this might add 5% or even significantly more to the technical provisions.

Limitations of reliance

- This presentation is prepared for the Trustee of the MNOPF, and others should not rely on it or take action based on it without seeking their own independent advice.
- This document sets out the results of the annual update, and it does not comply with the contents of the actuarial guidance note GN9. Its purpose is to illustrate the considerations involved in financing the Fund.
- The written comments included in this presentation should be considered in conjunction with the supporting and amplifying oral comments and background provided by Watson Wyatt prior to any actions or decisions being taken.
- The content of this presentation was based on our understanding of the Pensions Act 2004, Regulations, Codes of Practice, Guidance and other relevant information available at the time of preparation. This presentation may not reflect the position at any future date.
- This presentation should not be disclosed to any third party other than in accordance with the terms of engagement agreed with you or with our specific consent. Unless otherwise specifically agreed in writing we assume no responsibility, duty of care or liability to any third party who may gain access to a copy of this document.
- The assumptions made about future economic and demographic conditions are precisely that; they are assumptions, and not predictions or guarantees. They provide, we believe, a reasonable basis on which the Trustee can formulate their policy, but they must be aware that there are uncertainties and risks involved in any course of action. There is no guarantee that the assumptions made will be borne out in practice, and the expectation is that in actuality the Fund's experience will, from time to time, be better or worse than that assumed.
- We have based the calculations on audited asset information.



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30 October 2008