

Scottish Borders Pension Fund

2023 Actuarial Valuation

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Agenda

- Background to the actuarial valuation
- What's happened since 2020?
- 2023 valuation results
- Contribution rate setting
- Funding Strategy Statement (FSS)



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Please ask questions as we go



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Background to the actuarial valuation

Why we do a valuation?



Calculate employer contribution rates



Compliance with legislation



Analyse actual experience vs assumptions



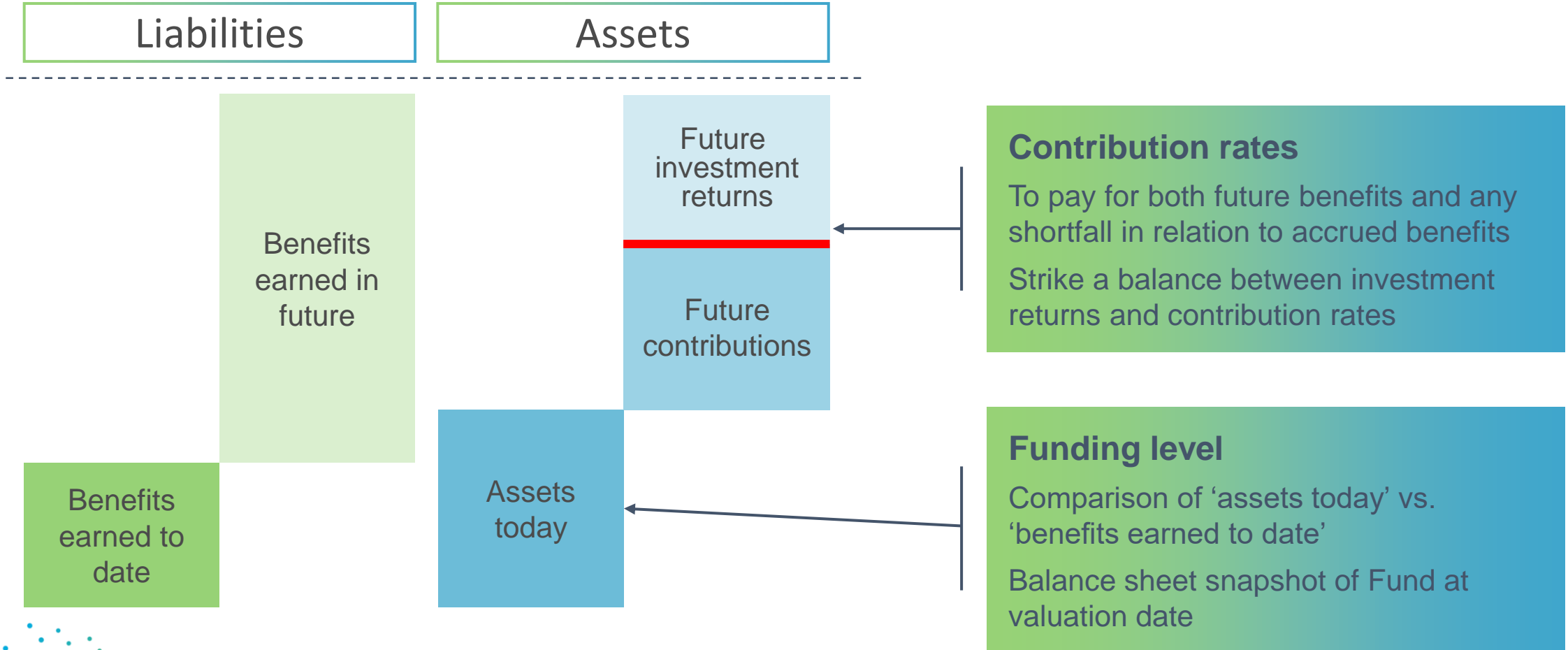
Review Funding Strategy Statement



Part of continual 'health check' on fund solvency

The triennial valuation is a key risk management exercise for the Fund

Background to the valuation



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What's happened
since 2020?

Wider funding context

Significant asset returns in first half of inter-valuation period, due to bounce-back from Covid-19 market fall in February-March 2020.

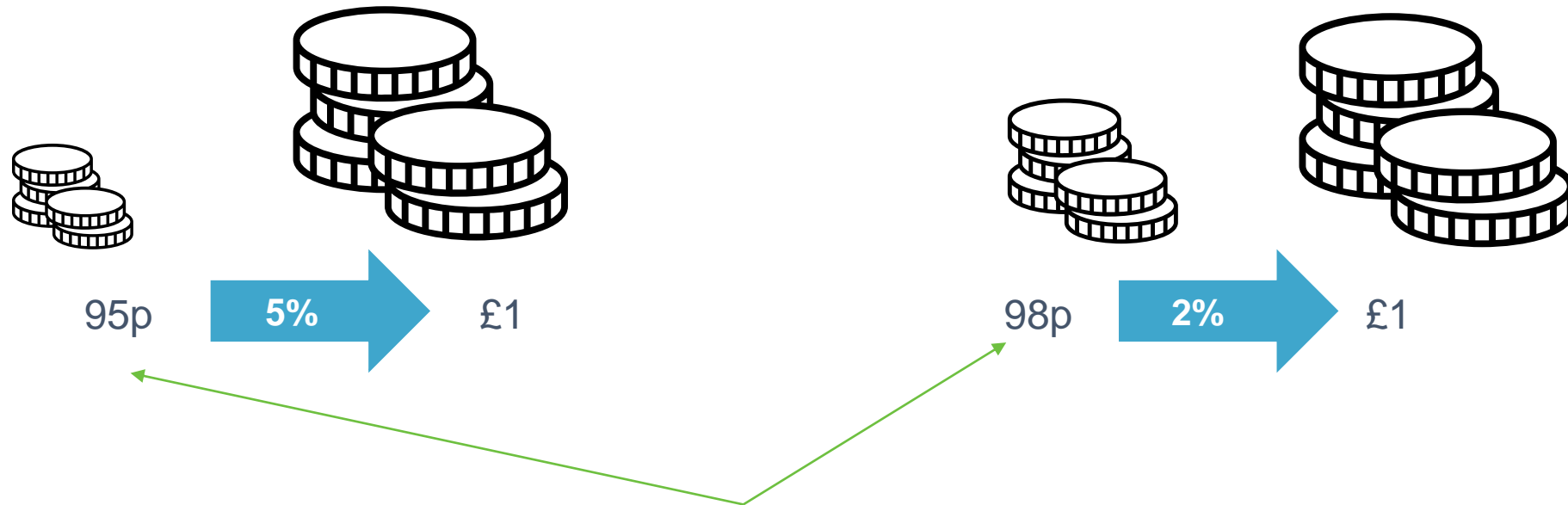
Material fall in liability values in second half of inter-valuation period due to rising interest rates.

Asset & liability progression – 2020 to 2023



Source: Hymans Robertson sample LGPS fund

Impact of future investment returns

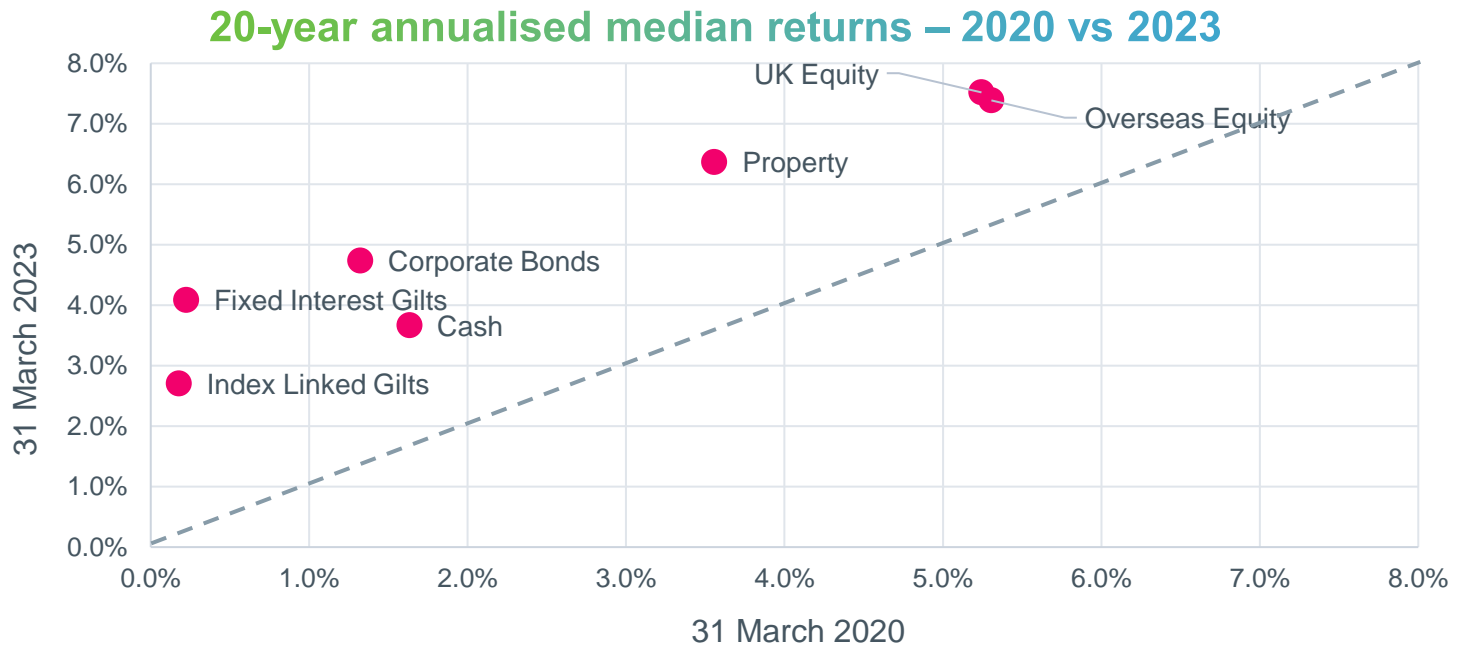


Different 'present value' of future payment under different future investment return assumptions

Investment return assumption places a 'present value' on future benefit payments

Future investment return expectations

- Used to project forward asset value in modelling
- Same model and approach as used for 2020 valuation
- **Higher return expectations** now compared to 2020
- Result of increases in global interest rates



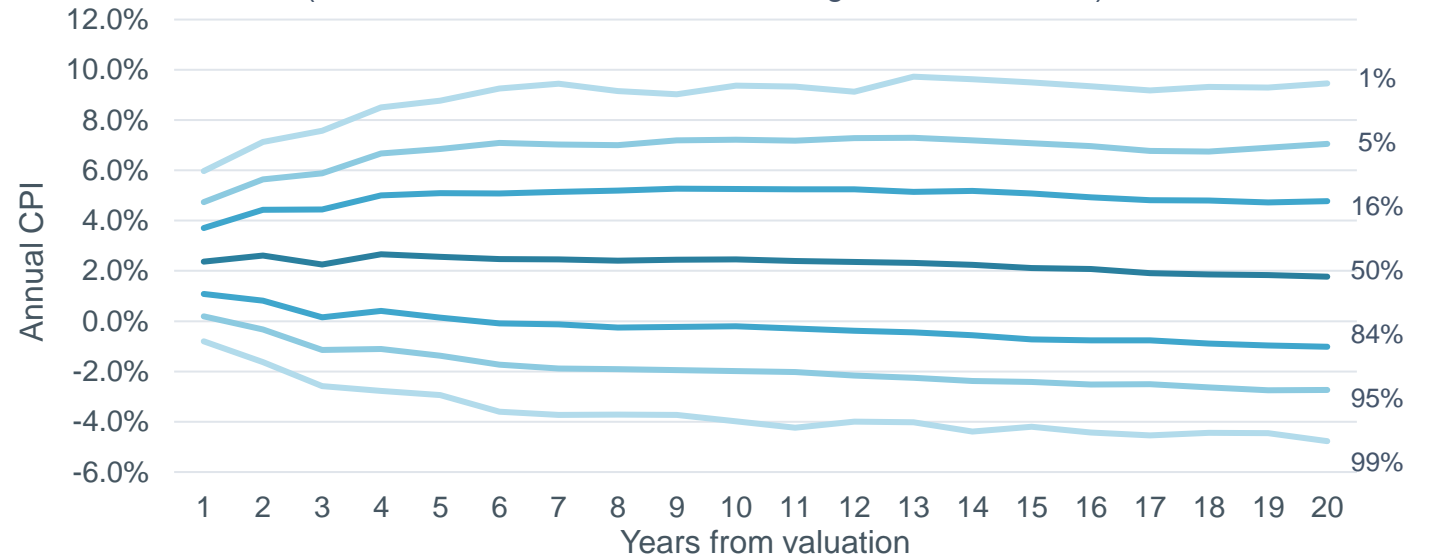
Positive impact on 2023 funding valuation results

Benefit increases

- LGPS benefits increase with CPI inflation
- Used to project forward benefits and contributions in modelling
- Similar approach as the 2020 valuation
- **Ongoing uncertainty around high inflation** captured via risk-based approach

Distribution funnel for CPI inflation at 31 March 2023

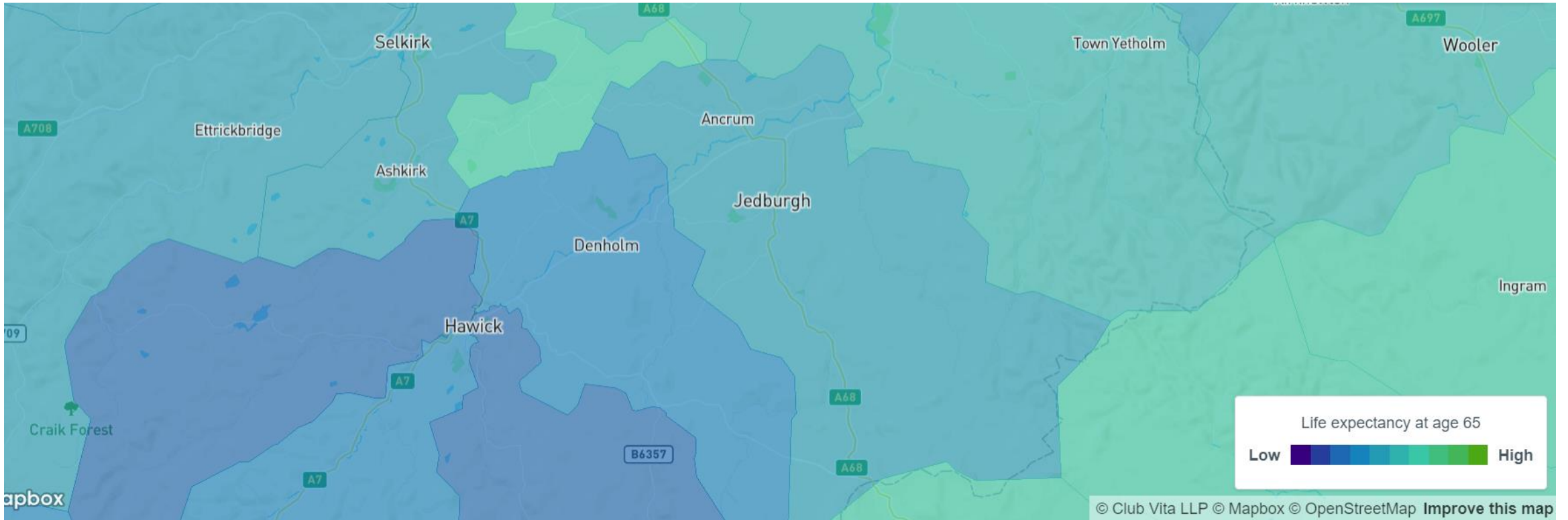
(RHS %'s are likelihood of inflation higher than this level)



Negative impact on 2023 funding valuation results



Longevity trends



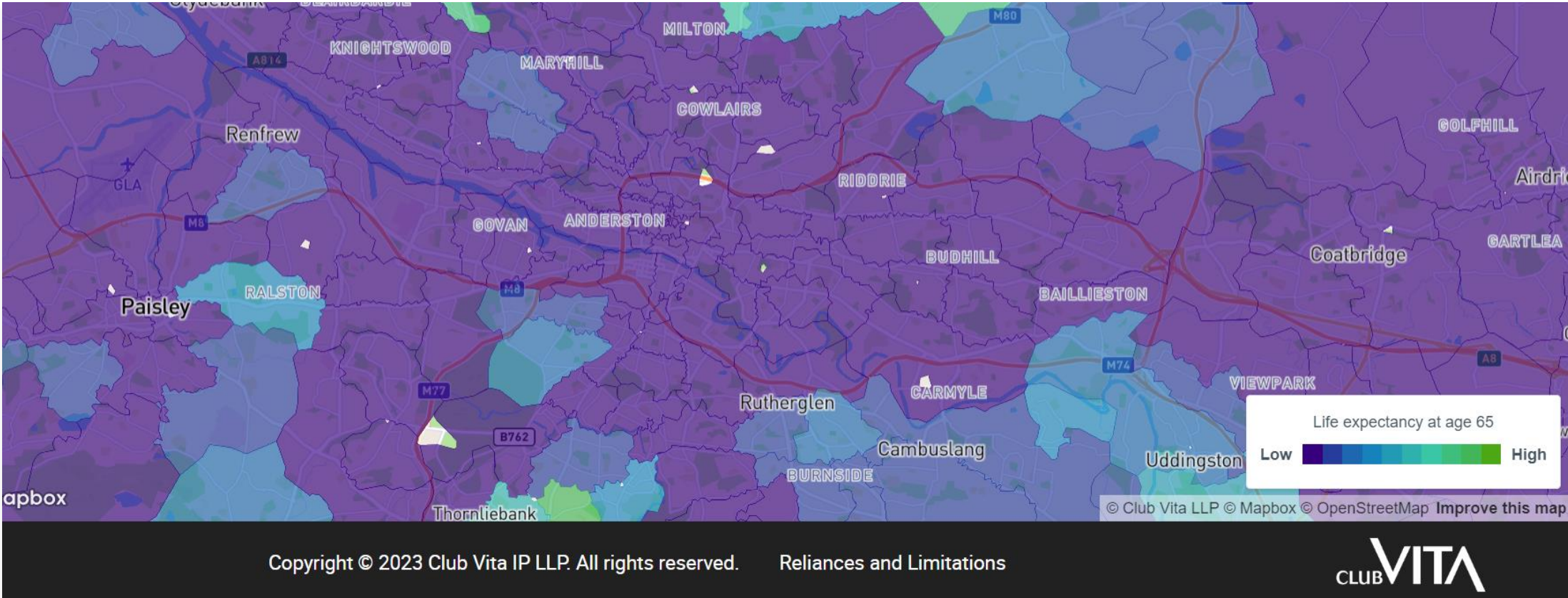
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Reliances and Limitations



Assumptions tailored specifically to Scottish Borders Council Pension Fund members

Longevity trends



“The Glasgow effect”

Key valuation assumptions at 2023

Financial assumption	31 March 2023	Required for	31 March 2020
Discount rate	5.2% pa	To place a present value on all the benefits promised to scheme members at the valuation date. The Fund's assets are estimated to have a 80% likelihood of returning above the discount rate.	3.8% pa*
Benefit increases/CARE revaluation	2.3% pa	To determine the size of future benefit payments.	1.9% pa
Salary increases	3.0% pa	To determine the size of future final-salary linked benefit payments.	2.6% pa

*Based on a 70% likelihood of success in 2020

	31 March 2023	31 March 2020
Male pensioner	20.6 years	20.9 years
Male non-pensioner	21.2 years	21.9 years
Female pensioner	23.3 years	23.5 years
Female non-pensioner	24.9 years	25.4 years

Pensioners are assumed to be aged 65 at the respective valuation date and non-pensioners are assumed to be aged 45.

Robust and evidenced based approach to agreeing assumptions

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2023 Valuation Results

Whole Fund funding level at 31 March 2023

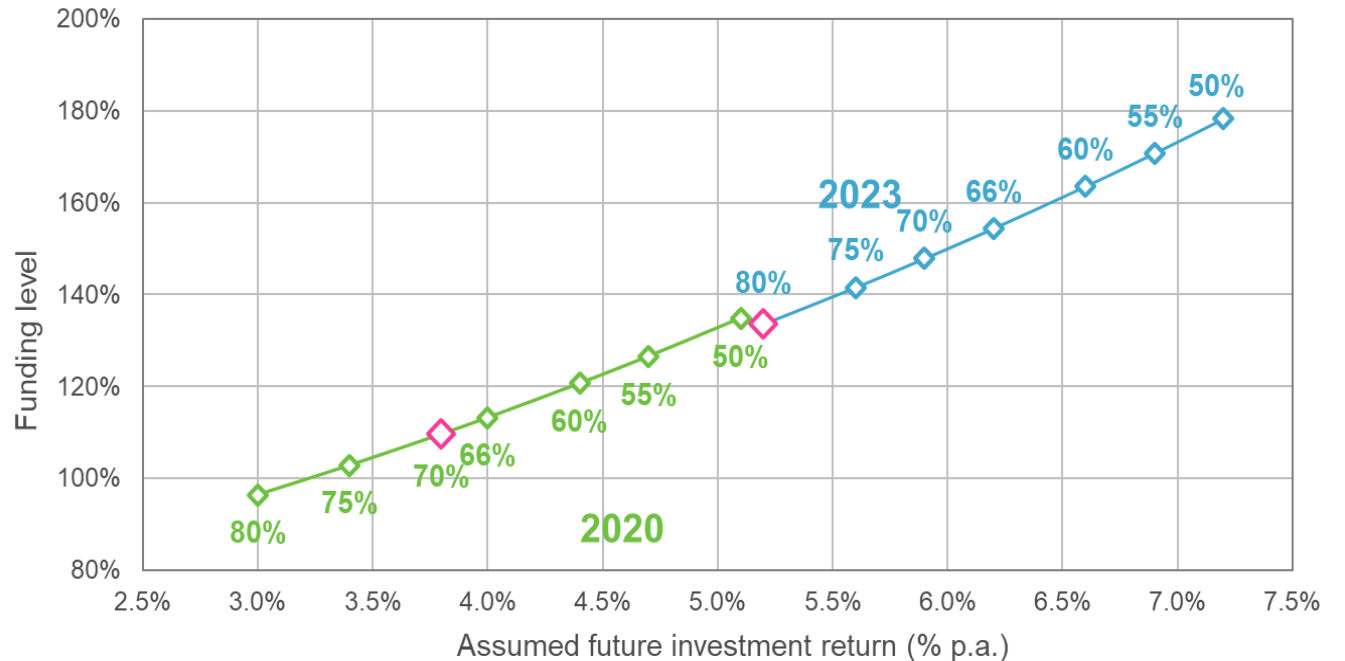
Valuation Date	31 March 2023	31 March 2020
Past Service Liabilities	(£m)	(£m)
Employees	238	259
Deferred Pensioners	91	94
Pensioners	320	296
Total Liabilities	649	650
Assets	866	713
Surplus/(Deficit)	218	63
Funding Level	134%	110%

Please note that numbers may not sum due to rounding

The reported funding level does not directly drive employers' contribution rates

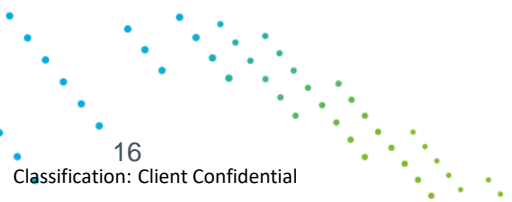
Measuring the funding position today

- The funding level is 100% if future investment returns are c3.2% pa.
- The likelihood of the Fund's assets yielding at least this return is around 95%.
- The comparator at 2020 was a return of 3.2% which had a likelihood of 76%.
- The funding position is stronger at 2023 than 2020.

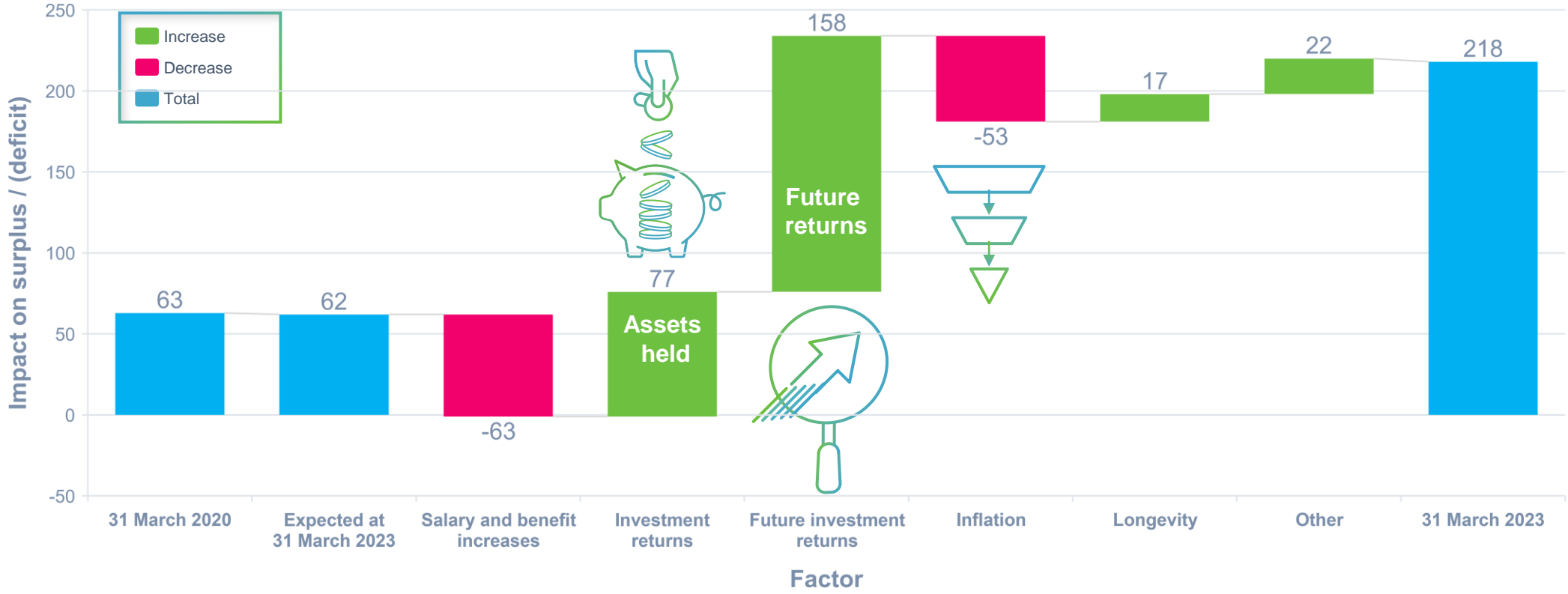


The pink diamonds show the 2020 and 2023 funding levels, with their associated likelihoods of success.

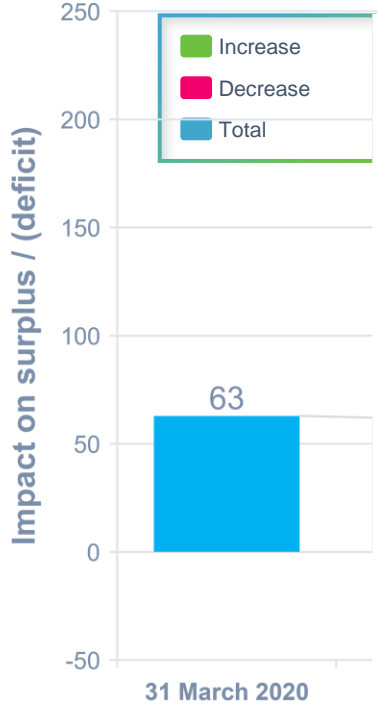
Positive impact on 2023 funding valuation results



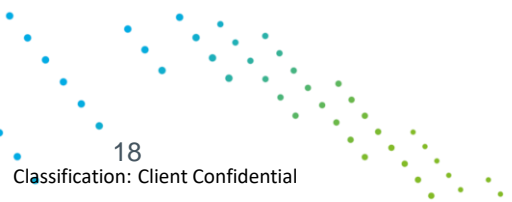
Changes since the last valuation



In summary....

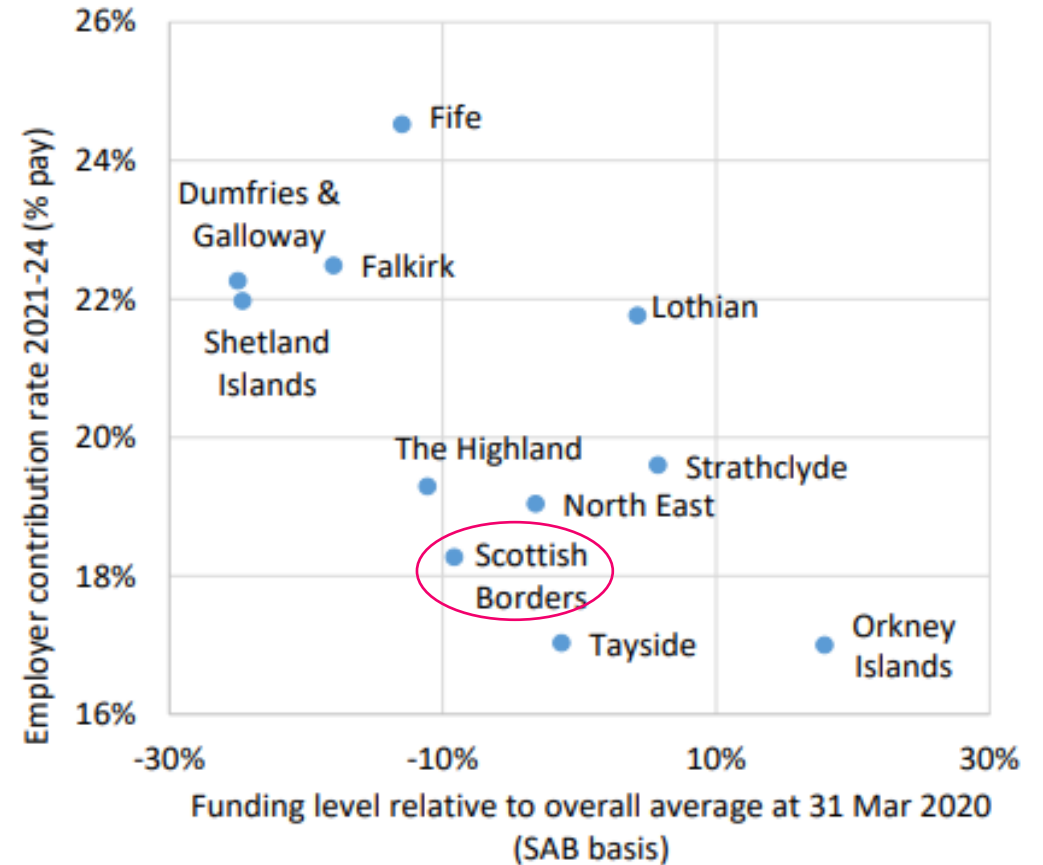


+
All other factors have a combined impact of £3m



2020 valuation – funding plan vs peers

- **Funding plans will differ** between individual LGPS funds as they have different funding positions, investment strategies and attitude to risk.
- **Your funding plan** should be set based on the Fund's own views around long-term funding robustness and employer affordability.
- However, we do acknowledge that employers and other stakeholders will **compare and contrast** with peers who may participate in other funds.
- A **high-level comparison between funds** is detailed in this chart showing how the average fund-level contribution rate varies with past service funding position.
- Note that this chart does not allow for differences in investment strategy or prudence levels. Therefore it should only be used for **high-level information** and not relied upon to make funding decisions.



Source: Government Actuary's Department, 2020 Section 13 valuation
[LGPS Scotland S13 Report as at 31 March 2020 \(publishing.service.gov.uk\)](https://publishing.service.gov.uk)

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Contribution rate setting

3 steps to setting the funding strategy



Funding target

What is the employer's funding objective?



Time horizon

Will the employer continue to participate in the Fund for the long term or will they exit (and when)?



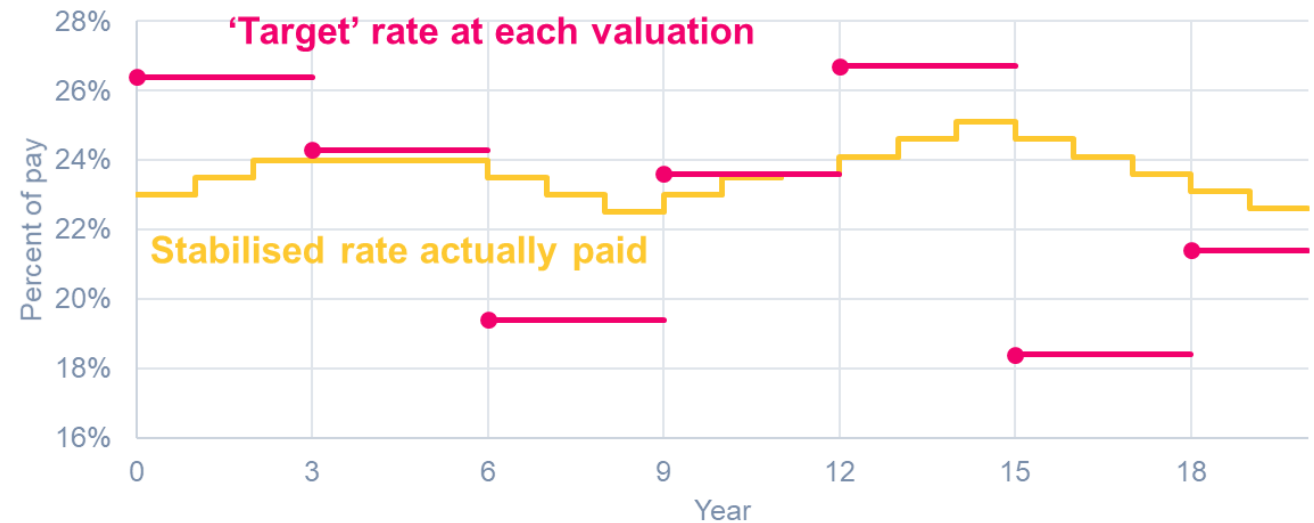
Likelihood of success

How strong is the employer's covenant?

Reflects the circumstances of each employer and allows the Fund to manage risk

Contribution Rate Stability Mechanism (CSM)

- The Fund operates a CSM for the Scottish Borders Council pool group of employers. Annual changes to rates are restricted to +/- 0.5% of pay.
- **Stabilisation takes a long-term approach** to setting contribution rates which cuts through short-term funding 'noise' ("underpay in the bad times, overpay in the good"). The chart opposite is illustrative only.
- It is an **explicit mechanism** documented in the FSS. At each valuation, the Fund must check that the funding plan remains appropriate and use that plan to set contribution rates for the Pool.



The CSM is designed to keep contributions stable through the peaks and troughs of market cycles

Tools for managing surpluses



Reduce employer contribution rates



Change the investment strategy



Increase prudence level



Retain the surplus

The funding level excludes the cost of future service benefits

Tools for managing surpluses



Reduce employer contribution rates

All employers expected to pay lower rates – subject to agreement



Change the investment strategy

Considering investment strategy with investment advisors



Increase prudence level

Minimum likelihood of success moved from 70% to 80%



Retain the surplus

Some surplus retention built into the contribution rate calculations

Factors considered at the 2023 valuation

- Avoid a **'knee-jerk' reaction** to the significant increase in surplus
- Almost all of the increase in surplus is due to **changes in liability assumptions** rather than actual investment performance
- The cost of funding future service benefits still must be met, with contribution rates reflecting **fairness of costs between generations**
- Market conditions and economic variables, such as interest rates and inflation, are **currently volatile**.
- In addition, there is **significant uncertainty** around climate and geo-political risks that may lead to future market *'shocks'*.

Aim is to apply a consistent and proportionate approach to funding plans across all Fund employers

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Funding Strategy Statement (FSS)

Key principles of the FSS

Setting out the Fund's approach to:

- Risk management
- Setting employer contributions
- Other important funding policies (e.g. employer cessation)

Governance process includes:

- Regulatory requirement to maintain the FSS
- Reviewed and updated triennially
- Consulted on with employers followed by approval by Committee

The Fund prepares, maintains and consults on the FSS in line with CIPFA guidance

Thank you

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