



## CENTRE FOR THE STUDY OF FINANCIAL INNOVATION

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**Managing longevity for pension funds. A round-table discussion with Douglas Anderson (Hymans Robertson), Andrew Reid (Credit Suisse) and Mike Tyler (Life Trust Insurance). Wednesday 19 November, 2008, at Waterman's Hall, 18 St Mary-at-Hill, London EC3R 8EF, 12:30-2:15pm.**

The first speaker began by explaining how pension funds tend to look at longevity in terms of their own experience, and not by looking at the experience of the pension fund community as a whole. As a result, the speaker said that his company had begun collating a database, which would allow schemes to look at longevity experiences across a much bigger pool of schemes. Ultimately, he explained, while everyone knows that longevity is increasing, no one knows if and when it is going to plateau or even start declining. But the more data that pension schemes have to try and make accurate assumptions about their members, the better.

The speaker said that his data has bit been showing the improvement in longevity that the traditional actuarial tables have been showing. In total, he said, the life expectancy of men at the age of 65 has increased by 3.3 years between 1993 and 2007, but by only 2.5 years for women – illustrating that the gap is narrowing between the sexes. This may be explained by more women smoking.

The speaker said the advantages of compiling such a large pool of data is that it eliminates the statistical noise, making it much easier to see trends. He said he hopes that this will be of use to pension trustees, for whom longevity is their second or third biggest risk, behind employer solvency and investment risk.

The second speaker said his company had focused on building a solution to help eliminate longevity risk – and was now starting to sell longevity swaps to pension schemes. These work by the pension fund agreeing to pay a premium each month, in return for which the provider will guarantee to pay for their pension liabilities. This allows schemes to fix their costs for a group of pensioners.

The speaker said that his company raises the money to pay the pension schemes from investors, who want exposure to mortality risk as an asset class. Investors are willing to come on board with a 20 or 30 year time horizon, which leaves his company only left with the tail-risk. He explained that the chief competitor to a swap is an annuity. The difference, however, is that an annuity is funded, whereas swaps are unfunded.

One member asked why not many schemes have bought swaps yet. The speaker said that they were still relatively new, and said trustees were suspicious of new products in the current market.

Another member asked whether it would be useful for the government to issue long-dated bonds which could cover the tail-risk that the speaker's company is left exposed to. He said

that such instruments could also be of use to the annuity market and could help maintain competitive rates. This would have the lateral benefit of keeping more people off government benefits in retirement.

The third speaker said his company had also launched a product to help mitigate longevity risk – but this product was specifically targeted at schemes where a few members posed a potentially disproportionate risk. For example, if 2 per cent of a scheme members were highly paid long-serving executives and consequently represented 30 per cent of the scheme liabilities, the scheme could run into severe difficulties if these members lived long lives.

Hence, the speaker said his company helps mitigate this risk by pooling these liabilities with other similar liabilities from other schemes – and provides an income stream, via a unit-linked annuity, which should cover any unexpected rise in liabilities. The scheme is then left with a much more regular risk profile, which will improve its chances of being able to sell itself if it so wishes. Furthermore, the capital outlay required is much smaller than other options for a scheme – costing just 0.2 per cent of the scheme liabilities. The speaker said the market acceptance of his product had been strong so far.

All three speakers concluded that what was needed most in the industry now was education. While there are a growing number of ways to mitigate longevity risk, many trustees were still unaware or do not fully understand them.

However, another member concluded the session by expressing some concern that by inventing products that “manage” the situation, the industry is endorsing it. Ultimately, the member said, schemes need to also make some hard decisions, and look at cutting back benefits for future members where they can.