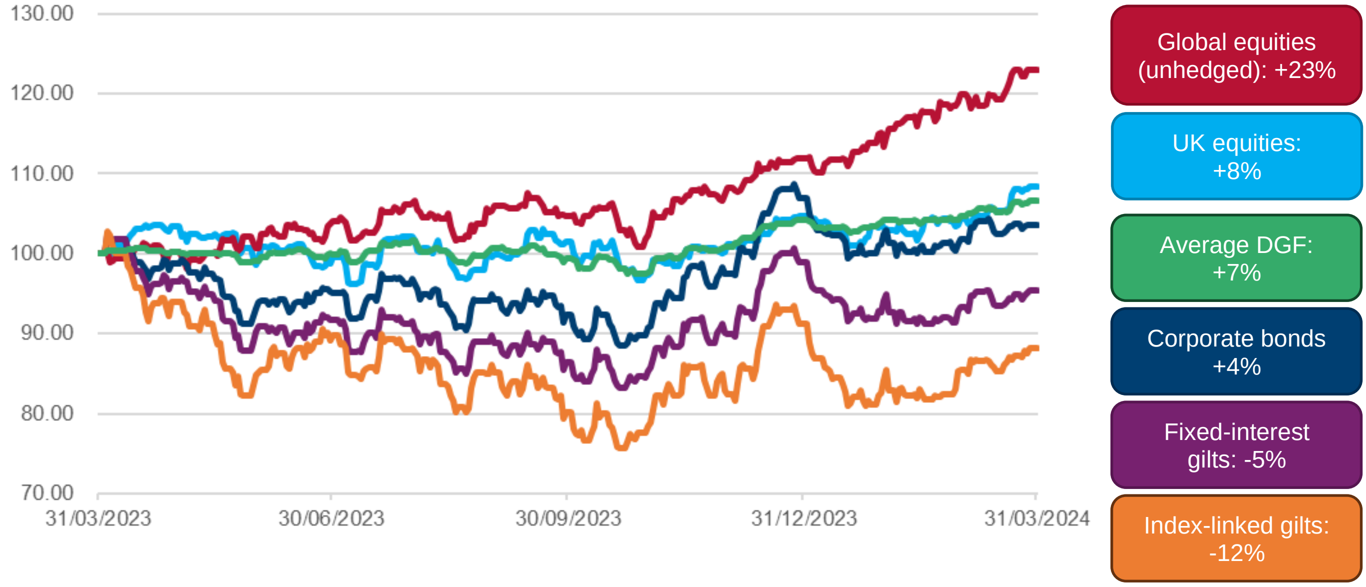
Housing briefing, May 2024
Pension cost accounting for housing associations

In this briefing, we look at the factors that will drive the changes to employers' pension cost accounting positions as at 31 March 2024.

Changes in financial markets

Global equities have been the standout performer over the past 12 months, with returns of over 20%. In a familiar story, UK equities have lagged behind, despite returning 8% over the year to 31 March 2024.

Government bonds have incurred losses of around 5% on fixed interest gilts and 12% on index-linked gilts over the year to 31 March 2024. Despite losses in Q1, corporate bonds have ended with a positive return of around 4% for the year, driven by falls in credit spreads.



Similar to last year, schemes (such as LGPS) aiming for good long-term growth with a high proportion of equities will have seen positive asset returns. Whereas schemes (such as SHPS) aiming to control risk by hedging gilt prices will have fared less well.

Changes to scheme liabilities

It may seem obvious, but scheme asset performance should not be considered in isolation. Changes in scheme funding levels will reflect movements in both assets and liabilities.

Bond yields

Longer-term corporate bond yields are slightly higher than they were 12 months ago – with an average increase of around 0.1% pa. In isolation, this will have a small impact on accounting liabilities, reducing them by up to 2%.

Inflation

Inflation remains higher than the Bank of England's 2% pa target, although the rate of price increases does now look to be slowing. How much of this is due to monetary policy and how much is simply down to a higher baseline is difficult to say. Interestingly, long-term gilt market expectations of inflation do not foresee a fall below 3% pa over the next 40 years.

The extent of any change to your scheme's liabilities due to actual inflation and shifts in expectations of future inflation will depend on the profile of the scheme and the caps and floors that apply to any inflationary increases.

Summary

The table below shows how key financial assumptions have changed over the year:

	31 March 2023	31 March 2024	Impact on the liabilities of an average[1] scheme
Corporate bond yield[2]	4.7% pa	4.8% pa	-1%
Gilt yield[3]	3.5% pa	4.0% pa	-8%
Market-implied inflation[4]	3.7% pa	3.6% pa	-1%
Actual inflation (year to March 2024)	RPI: 4.3% CPI: 3.2%		*Scheme-dependent*

1 An average scheme is taken to have a duration of 15 years and around 75% of liabilities linked to inflation
2 Yield on the iBoxx over 15-year AA-rated corporate bond index
3 Bank of England nominal gilt curve over a duration of 15 years
4 Gilt market-implied inflation at a term of 15 years from the Bank of England implied inflation curve

What does this mean for your scheme?

The impact on each scheme and liability measure will be different, although accounting liabilities are likely to be relatively unchanged over the year. Asset performance will vary significantly depending on scheme-specific investment strategies.

Those schemes (such as LGPS) that retain a material exposure to equities are likely to have seen improved funding levels, while those that are heavily invested in gilts (or LDI) to hedge changes in gilt-based funding liabilities (such as SHPS) may have seen their balance sheet position worsen due to the narrowing credit spread.

Next steps for year-end disclosures

Accounting assumptions are the responsibility of the directors of the participating employer. We are increasingly seeing auditors scrutinise how directors have chosen their pension cost accounting assumptions.

> You should set assumptions that are appropriate to your circumstances. This may not be the case for the default assumptions proposed by the scheme.

There is a range of assumptions that could be deemed appropriate and different actuaries and auditors may take varying views. The choice of assumptions can have a significant impact on your balance sheet at year-end and on next year's profit and loss account. We suggest you begin these conversations and consider taking independent actuarial advice as soon as possible.

Get in touch

For further information, contact our housing team or your usual First Actuarial consultant.