Trustee Newsflash!

SCHEME VALUATION SPECIAL September 2020

David Sims, Chair

Dear Members

A formal valuation of the final salary elements of the pension scheme normally takes place every three years. The current valuation (as at 30 June 2019), was formally signed off by the Trustees, the Company and Scheme Actuary on 17 September 2020.

The valuation is a complex process and takes a considerable amount of time to complete. The Pensions Regulator recognises it is a lengthy process so requires valuations to be completed within 15 months of the valuation date.

Now that we have the results the Trustees were keen to share them with you as quickly as possible so we have produced this Newsflash! to help you understand the scheme's funding position.

I hope that you find this a useful update, if you should have any questions please contact the ZPen Team at zpenteam@uk.zurich.com

ZPen funding level remains in surplus

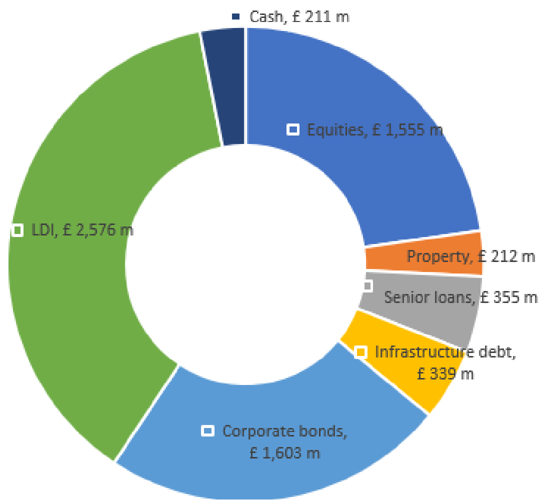
The formal valuation of the scheme that checks whether there is enough money to pay benefits as they fall due, or whether further contributions are needed, normally takes place every three years. At the last valuation (as at 30 June 2016) the overall position was a surplus of £304m on a technical provisions (TP) basis (a scheme funding level of 104.4% - that is assets were 104.4% of the liabilities). This includes the value of the Scottish Limited Partnership (SLP). The Statutory funding objective is the funding measure used for valuations under the Pensions Act 2004, such valuations are sometimes referred to as TP valuations.

The latest results show the scheme remains in surplus with a funding level as at 30 June 2019 of 100.8%. This is calculated including the SLP as an asset of the scheme. Without the SLP the scheme funding level has fallen slightly to 89.3%. More information about the SLP can be found later in this Newsflash!

Summary of the results of the valuation at 30 June 2019

Assumed cost of providing accrued benefits in respect of:	£m
Total liabilities (on a TP basis)	7,666
Market value of assets excluding SLP	6,849
(Deficit)	(817)
Funding level excluding SLP	89.3%
Value of SLP	880
Surplus including SLP	63
Funding level including SLP	100.8%

Market value of assets excluding SLP



NB: The pie chart does not include Net Current Assets and SLP

What happens next ?

Following a formal valuation it is normal practice for the Scheme Trustees to review the factors used when calculating members' benefits for consistency with the valuation assumptions. The Trustees recently kicked off this review

Want more information about the valuation results ?

A copy of the full valuation results can be downloaded from the Library section once you've logged in to the scheme website www.zpen.info

Investment Strategy

As part of the Trustee's Integrated Risk Management approach, the Investment Strategy was reviewed during 2020 alongside the 2019 valuation. As a result of this review the Trustee agreed to reduce interest rate and inflation risks further using Liability Driven Investment (LDI) and to increase ZPen's exposure to infrastructure debt. The implementation of this investment strategy began in Q3 2020 and it has been factored into the valuation process.

The Employer Covenant

As part of the valuation process the trustees are required to consider the employer covenant - the company's ability to support the scheme in the future. Through their ongoing work with PwC to assess the strength of the covenant, the Trustees have satisfied themselves of the Company's ability to support the scheme.

What is the Scottish Limited Partnership (SLP)?

The SLP is quite complex but involves loans guaranteed by Zurich Insurance Company in Switzerland which generates an annual income stream of £60m for up to 24 years from July 2014. The income stream will stop after 24 years, or sooner if certain funding conditions are met (or if certain prescribed events occur). As the SLP value at 30 June 2019 exceeds the value of the deficit excluding the SLP, it is providing the scheme with additional funding that it would not otherwise have access to.

An independent pricing agent values the SLP and the Trustee in consultation with the scheme auditors agrees this value. If the SLP should fail to operate as expected Zurich Financial Services (UKISA) Limited, the Principal Company, has agreed to ensure that the employers become responsible for continuing payment of contributions of at least £60m payable by 30 June each year.

ES Executives' section results

Assumed cost of providing accrued benefits in respect of:	£m
Deferred members	8.9
Pensioner members	172.6
Total expected cost	**181.5**
Market value of assets	**199.4**
Surplus/(Deficit)	**17.9**
Funding level	**110%**

The ES Executives' section is separate to ZPen but the valuation date is the same, at 30 June 2016 this section had a surplus of £1.6m, a funding level of 101%.

The position at 30 June 2019 has improved compared to 2016, with the funding level now at 110%. As this section of the scheme remains in surplus, the Trustee and the Company have agreed no annual deficit funding contributions are necessary.

Comment from the Scheme Actuary on the valuation results for the final salary elements of the scheme

Susanna Morran

"As Scheme Actuary, I have a professional duty to advise the Trustees on the funding of the Scheme. This includes advice on the various assumptions which need to be made to value the Scheme's liabilities, such as expected longevity of members and future investment returns. Due to the uncertainties involved, these assumptions incorporate appropriate levels of prudence. Having carried out the formal review as at 30 June 2019, I am satisfied that the results give a fair view of the funding position of the Scheme."

COVID-19

In early 2020, the COVID-19 pandemic resulted in a period of uncertainty for the global economy and financial markets, in turn creating significant volatility in the valuation of investment assets, including fluctuations from the impact in foreign exchange rates. The longer term impact of COVID-19 is unknown, the Trustee will keep the situation under review over the coming months, including the implications for investment strategy and risk management.