Concept of a Stress Test for IORPs

Pensions Stress Test & Quantitative Assessment
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Stress test objectives

- Provide insight and raise awareness of the occupational pensions' sector risks and vulnerabilities
- Assess the resilience of IORPs and their pension schemes to adverse market scenarios and a longevity scenario
- Evaluate potential transmission mechanisms of IORPs to the rest of the financial sector and the real economy

Stress testing components

The IORP stress test constitutes a European-wide exercise, including all EEA countries with material IORP sectors and covering all types of IORPs

The stress test consists of

- Core module for IORPs providing defined benefit (DB) or hybrid schemes
- Satellite module for IORPs providing defined contribution (DC) schemes

Core module

- The resilience of IORPs providing DB/hybrid schemes will be assessed using:
    1. Non-harmonised valuation standards in accordance with the national prudential regime
    2. The holistic balance sheet valued on a market-consistent basis (allowing European comparison)
- Assessing the gap between assets and liabilities under different adverse scenarios
- Under holistic BS valuation PV(Assets) are compared to PV(liabilities)

Core module – risks evaluated

- The impact of instantaneous market stress scenarios at the reference date of 31 December 2014 will be evaluated
  - Risk free curve
  - Inflation curve
  - Sovereign bond yield
  - Corporate bond yields
    - Financial – unsecured, covered bonds
    - Non-financial
  - Equity shocks (EU developed market, non-EU developed, emerging)
  - Alternative investments – private equity, commodities, hedge funds
  - Exchange rate shocks
  - Credit spreads
- Longevity scenario

Core module - questionnaire

- The stress test framework includes a qualitative questionnaire
- The aim of the qualitative questionnaire
  - To gather background information on the calculations performed
  - To gain insight in possible transmissions in the adverse market scenarios to other parts of the financial sector and the real economy (second round effect) – for DB only

Note: EIOPA webpage contains links to PDF files (with instructions, not to be filled in)

- DB: excel file + word document
- DC: excel file only

Satellite module – DC scheme

- The impact of adverse market scenarios on future retirement income for representative plan members will be evaluated
  - 35, 20 and 5 years to retirement respectively
- Formally, future value of cumulated contributions is equal to present value of future benefits at the retirement age
- Based on this identity implied benefits under baseline and adverse scenarios will be compared
- Exploring the potential implications for the real economy

Satellite module – scenarios

- Instantaneous market stress scenarios similarly as for DB are considered
- Low return scenarios - downward shift in risk premiums on fixed and non-fixed income asset classes
- Longevity scenario - impact of an adverse longevity scenario on future retirement income - assumed to be independent of the adverse market scenarios

Thank you

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