6.

Pensions & Financial Stability

OPSG Response to EIOPA Financial Stability Report (December 2016)

April 26, 2017

EIOPA Report

- Presentation by Petr Jakubik
- Distinction DB-DC maybe too strict:
  how about CDC, DA, and hybrids?
- Stress test 2017 will provide more insights into IORPs vulnerabilities and financial stability risks, as well as impact on the real economy
  → second round effects

Stability concepts

- Micro: financial health of individual pension funds / IORPs
- Macro: financial health of economy as a whole

- 2 way relationship:
  - From macro to micro: EIOPA report (mainly Ch.4)
  - From micro to macro: feedback statement

Micro stability

- Impact on individual IORPs of:
  - Low interest environment
  - Low returns to financial assets
  - Meeting future obligations is challenging
  - Risk of “search for yield”
- Menu of options differs across countries
  - Sponsor contributions
  - Member contributions
  - Reduction of benefits
- No coverage rate issues for iDC by definition
  - But plan may not meet expectations → trust gap

Macro stability

- Symmetric independent investment decisions
  e.g. hedging
- Regulation induced behavior
  e.g. derisking, implementing UFR
- Impact on real economy, e.g. mortgages, labour market, aggregate demand, wage rates / wage inequality
- Influence on prices of financial instruments

SWOT

- Opportunities:
  - pension money drives the real economy, e.g. sustainable investment
  - Illiquid investments provide stability, e.g. mortgages and real estate
- Threats:
  - Impact of the discount rate for liabilities on the economy
  - Risk based solvency requirements: procyclical

Final remarks

- EIOPA financial stability report 2x / year
- Suggestions for next issue:
  - Market structure → impact on systemic risk
  - Which accounting method balances stability with reality?
- IORPs are more stable than other financial institutions
- Macro financial stability risks are most prominent in countries with very large pension funds, e.g. UK, NL (= 83% of EU pension assets)