Nottinghamshire County Council

Report to Pensions Sub-Committee

8 May 2014

Agenda Item: 7

REPORT OF SERVICE DIRECTOR – FINANCE & PROCUREMENT

CASHFLOW MODELLING

Purpose of the Report

1. To inform members of the projected cash flows of the Fund.

Information and Advice

2. The latest triennial actuarial valuation shows that the Fund is in deficit. This deficit will be recovered by a combination of additional employer contributions and investment returns. In order to maximise investment returns (within acceptable risk parameters) the Fund's Statement of Investment Principles sets a long term investment strategy that favours growth assets (equities and property) over defensive assets (bonds and cash). However, this strategy is only possible if the Fund is able to cover pension payments without recourse to selling assets.

3. Prior to 2010/11, the Fund regularly received net additions from members (contributions received less benefits paid) in excess of £30m a year. Since then, through a combination of reductions in active members and increases in pensioners, this position has deteriorated significantly. The position over the last five years is shown below.

	2012/13	**2011/12**	**2010/11**	**2009/10**	**2008/09**
Net additions from members	£5m	£17m	£24m	£48m	£50m

4. In addition to these net contributions, the Fund also receives substantial investment income. This income (net of taxes and investment management expenses) is shown below for the same period.

	2012/13	**2011/12**	**2010/11**	**2009/10**	**2008/09**
Net investment income	£84m	£80m	£74m	£74m	£78m

5. In order to continue with a long term investment strategy, it is increasingly important to be aware of the projected cash flows of the Fund. Attached is a report from the Fund's actuary that models future cash flows over the next 20 years. The report shows projected cash flows in four scenarios as follows:
    1) Stable active membership
    2) 20% reduction in active membership over next 3 years
    3) Scenario 2 plus 1% reduction in income yield

4) Scenario 3 plus CPI inflation 1% higher

6. In all four scenarios, net additions from members are predicted to turn negative in the near future. However, overall cash flow remains positive through the 20 year period in scenarios 1 and 2. In scenario 3, cash flow turns negative in 2024. In scenario 4, cash flow turns negative in 2021.

7. It is very unlikely that active membership will remain stable, particularly over the short term as there are likely to be further reductions in active membership as a result of continuing efficiency measures within the public sector. Income yields are at their current levels following the most severe economic downturn in recent history and there is no indication that these will reduce significantly below this level. The level of inflation has recently fallen below the Bank of England's target of 2% and the Bank has stated that it expects interest rates to remain at low levels for some time to come. Arguably, therefore, scenario 2 is the most likely.

8. Scenario 2 shows that the Fund is unlikely to need to sell assets to fund benefits for at least 20 years and this allows the Fund to continue with its long term investment strategy. The cash flow position will continue to be closely monitored.

Statutory and Policy Implications

9. This report has been compiled after consideration of implications in respect of finance, the public sector equality duty, human resources, crime and disorder, human rights, the safeguarding of children, sustainability and the environment and those using the service and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

RECOMMENDATION/S

1) That the report be noted.

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For any enquiries about this report please contact: Simon Cunnington

Background Papers and Published Documents

Except for previously published documents, which will be available elsewhere, the documents listed here will be available for inspection in accordance with Section 100D of the Local Government Act 1972.