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Sixty second summary

2022 valuation results – early insights

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The end of summer holidays in a LGPS valuation year not only heralds the start of school, but also delivery of the first few whole fund level results. We've studied these results and some common trends are emerging. These are shared in this note to give your own results more context or, if we're still working through the data and calculations, give you an indication of what to expect.

The headlines

It's been discussed in many forums by many different stakeholders, so it should come as no surprise that the big headline from the 2022 valuation is a strong improvement in the past service funding level. The question was just how much of an improvement. **The early results show a funding level increase of around 7-12%.** This is great news for the LGPS, continuing to build on the improvement in funding over the last decade.

What's driving the improvement?

The reasons for the improvement fall into two camps:

1. Actual events since the last valuation being different from what was expected
2. A change in the outlook for the future

Actual events

The biggest single funding event since 2019 has been strong investment returns. The average investment return since 2019 from our sample has been c.28% (8.5% pa), with one fund returning in excess of 30%. **These excellent levels of returns have improved the funding level by around 15%.** For one county council fund in our analysis, higher-than-expected investment returns improved the funding position by more than £500m.

Whilst other events since the 2019 valuation have had little impact on the funding level, analysis of the experience shows some interesting trends:

- Mortality – a lot of focus has been on what the Covid-19 pandemic may mean for funding. Despite the harrowing level of excess deaths in 2020 and early 2021, the first sets of results show the level of

pension ceasing not being materially higher than expectations. **The impact on the funding position has been less than 0.1%.**

- Ill-health retirements – the number of these retirements has been steadily reducing over the last 10-15 years. Some funds have seen this trend continue, whilst others have seen an increase (the reasons for this may be linked to Covid-19). However, **when translated to the impact on funding at whole fund level, the outcome is consistently less than 0.25%.**
- Salary increases – these have been consistently higher than expected for all the funds in our analysis. Actual increases have been between 4.4% to 5.3% pa (compared to an average expectation of c.3.5% pa). This experience is also higher than what we've observed at the last couple of valuations. The knee-jerk reaction may be to conclude a relaxation in pay restraint, however the actual reason may be more nuanced and due to a 15% increase in the National Living Wage between 2019 and 2022. Despite the significantly higher than expected increases, **the impact on the funding level is only a reduction of around 0.7%** (reflecting the shrinking proportion of final-salary linked liabilities in the LGPS).
- Benefit increases – unlike salary, increases in CARE pots, deferred pensions and pensions in payment have been lower (c.0.5% pa) than expected due to the low levels of inflation in 2019/20 and 2020/21. This affects a larger proportion of a fund's liabilities and **so the impact (around a 1.2% funding level improvement) has generally more than offset the high salary increases.**

Future outlook

Assumptions around life expectancy and salary increases have seemed to remain broadly steady, resulting in minimal impact on the funding position. The biggest change in outlook is reserved for inflation; an average increase of around 0.4% pa across the duration of the liabilities to reflect the current high-inflationary environment. **This increase alone reduces the funding level by around 7-8%.**

Changes in the value of the discount rate (assumed future investment return) have been variable between funds, reflecting their different asset allocations, changes in return expectations for each asset class and whether there has been any change to the long-term strategic asset allocation since 2019. A LGPS fund's prudence is also incorporated into this assumption. No funds in our analysis have reduced the level of prudence for the 2022 valuation.

There has been a c.10% increase in the number of membership records (compared to the last valuation) for every fund in our analysis. This increase in records places yet more burden on LGPS funds' administration teams. Looking forward, this burden may be further increased from higher than normal opt-outs as a result of the current cost-of-living issues. If there are significant numbers, this could also impact a fund's net cashflow position (which could also substantially change depending on the 2023 pension increase order).

Good news for employers?

Yes – it's much better than a fall in funding level!

However, funds should be cautious about getting too excited at this stage. The past service funding position (focus of this analysis) does not directly drive employers' contribution rates. Additionally, this analysis is at whole fund level and results will vary (in some cases, significantly) between employers depending on their own experience.

After calculating the initial whole fund results, the next stage is to calculate individual employer funding positions and contribution rates. For some funds we will be doing this over September and, as we did for council contribution rates and whole fund initial results, we will share the early insights at our next valuation webinar on 7 October – keep an eye out for the invite!

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