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Perspectives on Defined Contribution Pensions in the EU

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DC Investment Strategy

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Important Notes

The views expressed in this presentation are those of the presenter(s) and not necessarily those of their employer.

This does not contain investment advice relating to your particular circumstances. No investment decision should be made based on this information without first obtaining appropriate professional advice and considering your circumstances.



Evolving European Regulatory Context

- IORP II Review
- Capital Markets Union

Ongoing IORP II Review: Main Headwinds

Savings & Investment Union

Free up pension schemes to support SIU objectives

- Draghi Report – unlock pension savings for productive economy
- “Long-term investor” language in IORP II:
 - “the assets shall be invested in the best long-term interests of members and beneficiaries as a whole”
 - “other instruments that have a long-term economic profile and are not traded on regulated markets”

SIU Dual Purpose:

1. **Savers:** Facilitate pension savings & grow participation
2. **Companies:** greater access to capital / investment in private assets

UK also seeking to unlock (DC) pension funds:

- New LTAF fund vehicle (“Long Term Asset Fund”) developed to support DC usage of private market / less liquid assets



Ongoing IORP II Review: Main Headwinds

Transition DB to DC

Increasing focus on protecting the member, rather than the IORP

1. Product Oversight & Governance / Duty of Care towards members
2. Member communications, Financial Education & projections
3. Transparent, Cost & Charges
4. Long-term risk assessment
5. Governance

- **Projections dual purposes:** both for member communication (2) and as an internal risk management tool (as part of “Long-term risk assessment”)
- Focus on **Member Risk Tolerance** throughout recommendations
- **Focus on Member outcomes** as key metric (POG, ORA, Long-term risk assessment)
 - PEPP example – Capital Guarantees / Satisfy expected outcome criteria



Key Influences on Investment Strategy

- Scheme Design / Member Circumstances
- Member Objectives
- Member Risk Tolerance

What do we mean by Defined Contribution:

Many different structures across Europe



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Scheme Design

Member Circumstances

Linked to Employer?

Provided by employer

Link to Profession / Industry

Individual Produce

Fund for Life

Purpose / Interaction with Other Benefits

Supplemental to DB / State Pension

Only / Main Benefit

Top-Up

Form of Benefits

Mandatory Annuity

Member choice:
Drawdown / Cash / Annuity

Cash at Retirement

Drawdown

Pre-retirement or through Retirement?

Investment Return / Guarantees

Individual Account

Pure DC

Capital Guarantee

Guaranteed Minimum Return

Smoothed Returns

Collective DC

Pooled Investment

External Influences?

Other assets

Home-ownership

State Benefits

Earning Potential

Job Security

Dependants

Knowledge Level



What do people want from their Pension?

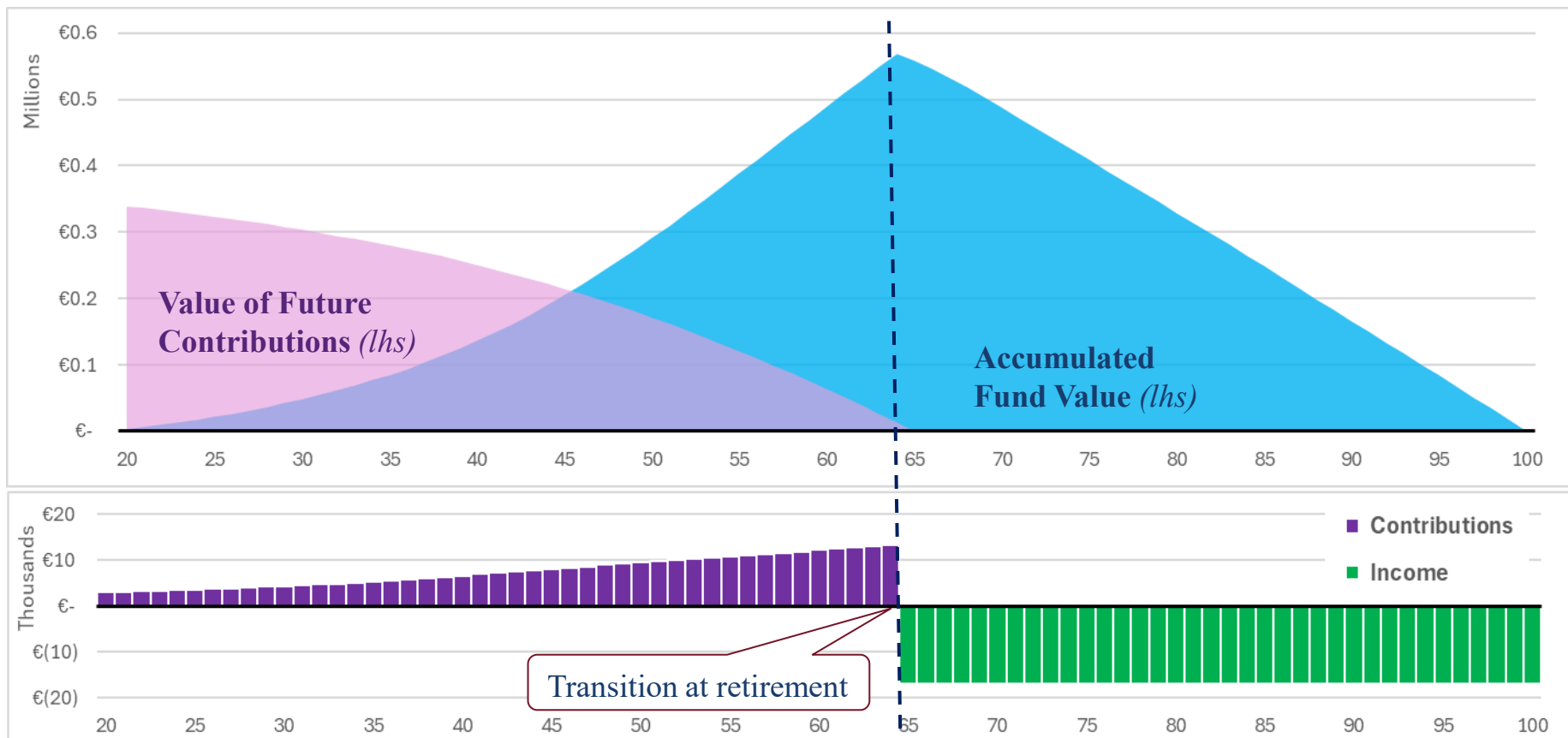
| Member Objective | Requirement | Risk to Members |
|---|--|--------------------------------------|
| Provide an adequate retirement income | • Keep pace with inflation | Inflation Risk Net Capital Growth |
| | • Cost effective and value for money | |
| | • Affordable contributions | |
| Provide a dependable retirement income | • Last for my lifetime | Longevity Risk |
| | • Manage exposure to market volatility | Sequencing Risk |
| Flexibility | • Enable people to choose their own investments to align with risk appetite | Challenge to risk sharing |
| | • Allow people to adjust timing / amount of income to meet their needs over time | Sequencing Risk Anti-selection |
| Provide protection for Life Events | • Protection for dependants | Mortality Risk |
| | • Provide income on disability | Disability Risk |

Changing Risk Profile / Risk Tolerance



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Evolution of Main Risk throughout pension journey



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Longevity

Fund Value

Volatility

Inflation

Net Investment Return

Challenging to manage
longevity as an individual

Need an income / withdrawals
Volatility could hurt fund
Still need return / inflation protection

Medium / Long investment horizon
Can tolerate more asset volatility
Prevent inflation eroding value

Operational, Liquidity, Communication, Security etc.

20 25 30 35 40 45 50 55 60 65 70 75 80 85 90 95 100

Investment Options for managing this risk



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| | Adequate Retirement Income | | Dependable Income | | Flexibility |
|--|---|---|--------------------------------------|-----------------------------------|---|
| | Affordable contributions | Inflation protection | Manage exposure to market volatility | Last for my lifetime | Investment choice / income / timing |
| Annuitisation at retirement | Higher fund required | Depends on annuity | Yes, post-retirement | Yes | Illiquid |
| | | | Interest rate risk at purchase | | |
| Balanced Fund throughout | Even risk throughout | Broadly Inflation Aligned | Managed but not eliminated | Individuals need to manage income | Yes Although need a buffer for longevity |
| Life-cycle investments | More Risk earlier when capacity is higher | | | | |
| CDC / Risk Sharing: (investment / longevity / both) | Pooling of risk | | | Diversifiable risk | Less flexibility |
| | Potential issues if population is aging | Potential for intergenerational cross-subsidy | | | |



Investment Challenges, as we look to Broaden Participation



How to help individuals to manage their longevity?



Is there a better way to provide growth and inflation protection, particularly in the early / middle years?



How to manage risks in the run up to and post retirement?



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