

DO NOT LET A SHOCK, SHOCK YOU

MarketMingle Amsterdam 2024 Discussion Highlights

Northern Trust was delighted to be joined by our clients, speakers from the Dutch pension industry and our Banking & Markets team at our latest networking event for front office professionals.

MarketMingle Amsterdam June 2024 focused on the theme of risk mitigation with our panel of experts exploring preventative measures and solutions to consider as the Dutch pension industry transitions to Wet Toekomst Pensioenen.

Panel Discussion Highlights

Managing Risk Through a Black Swan Event

The backdrop to our panel discussions centred on the hypothetical scenario of a market crash taking place during the transition to the new collective direct contribution model with schemes expected to face the following market challenges in such a situation:



Factors impacting schemes in this scenario included lower interest rates, increasing liabilities and reduced coverage ratios.



Equity and credit market declining which further lowered asset values and coverage ratios.



Market volatility surged, increasing risks despite some interest rate risk hedging.



Some pension funds expected delays or cuts in benefits due to breached coverage ratio thresholds.



Public concern growing about pension safety and adequacy amid market risks.



Expectation that regulatory scrutiny increased focusing on pension fund scenario planning and risk protections.



If this hypothetical scenario became a reality, what are some preventive measures and solutions that pensions can have in place to help mitigate risk?

- The presence of a thorough transition plan is crucial: Including timing of transition, and actions before and after transition.
 - A long-term view is essential: Shift in regime requires hedging against potential downturns.
 - Non-linear products are an option to consider when hedging potential downside risks.
 - Scenario planning is an important part of preparation to properly assess coverage impacts under adverse scenarios.
 - Board discretion: Deciding on risk mitigation measures based on scenario outcomes.
 - Remain flexible in adjusting protection strategies over time.
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How do you ensure a balanced outcome with regards to the governance within the pension fund?

- Governance is crucial and includes multiple factors.
 - Board education: The board needs an understanding of financial instruments.
 - A toolbox must be in place to enact the recommendations of the board. Process for toolbox readiness includes:
 - Initiate advisors for scenario planning and hedging options assessment.
 - Understand the impact: Evaluate various stress scenarios and their implications on portfolio.
 - Formulate a strategy: For example, agree on a hedging strategy balancing immediate action versus timing closer to transition.
 - Engage external advisors: Discuss trade-offs and customise plans based on expertise and flexibility.
 - Implement timelines: For example, acknowledge the time needed to set up and scale hedging strategies.
 - Preparation is also key, so having contractual arrangements in place for swift risk mitigation is important. For example, ensure contracts are in place for required financial instruments.
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How do you measure and mitigate risk?

- Know what is in your portfolio and what could happen in different scenarios.
 - Work with advisers and run scenarios so you can understand what would be the impact of different stress scenarios.
 - Know how different options for managing risk interact with each other.
 - Agree to a strategy but remain flexible to be able to adapt accordingly.
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How do you maintain control of the overall risk of the entire investment pool?

- It is imperative to be fully aware of how risk will react with a given portfolio.
 - Understand investment decisions to avoid unintentional risk and outcomes.
 - With heightened customisation levels, portfolios can be adapted to individual needs, but the risk should be intentional.
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How could you manage risk and overall risk exposure in today's geopolitical and regulatory environment?

- A new landscape is emerging for the front-office, offering new opportunities and challenges.
 - Mitigate associated trade risks by considering using a variety of service providers in the market.
 - Service providers can offer bespoke solutions that may address specific trading concerns, helping to mitigate risks effectively.
 - For example, a manager could utilise outsourced trading to ensure regional coverage and backup broker support for business continuity planning.
 - To support regulatory challenges, outsourced providers offer robust broker infrastructure and comprehensive service oversight.
 - Tailoring solutions can also help cater to specific needs, including new asset class trading and risk management strategies that align with client objectives.
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What is the importance of a transition manager, especially in a volatile environment?

- Transition managers are well positioned, given their depth and breadth of experience, to manage the complexities of transitioning investments. For example, transition managers can help clients navigate challenges like due diligence, manager replacements, and market volatility.
 - Help minimise risk and disruptions during periods of change.
 - Heightened expertise can help address unforeseen challenges and offer tangible solutions.
 - Implement controls and contingency plans when unintended market issues arise.
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How important is it to understand the risks within your investment portfolio?

- Important to be aware of where risks lie across the portfolio.
- Accumulating various exposures requires careful monitoring to understand their combined impact.
- Service providers can complete a portfolio analysis to identify and deliberately bucket risks, ensuring intentional risk management strategies.



How has the evolution of operating models impacted risk management?

- As operating models evolve, it is important to find strategic partnerships that offer efficient solutions.
- It is crucial to explore and determine the optimal operating model for your organisation.
- Understanding your current position and the improvements you need to make is essential for effective risk mitigation and operational efficiency.



For More Information

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