Royal Mail adopts ‘Collective’ DC; NEST to hold private equity

By Editorial Staff *Tue, Oct 5, 2021*

Royal Mail is converting its defined benefit pension plan to Britain's first "collective defined contribution" plan or CDC. In other UK news, the National Employment Savings Trust, or NEST, said it will invest 5% of its AUM in low-fee private equity.

The Royal Mail, Britain’s mail and parcel delivery service, aims to launch the UK’s first occupational “collective defined contribution” (CDC) plan next year, if government regulations on the new vehicle are published as expected this autumn, according to a report in IPE.com.

The CDC will supersede the Royal Mail Pension Plan, a defined benefit (DB) plan with £11.4 bn in assets and 124,000 members. It closed to accrual of career salary benefits in March 2018. A CDC plan is an alternative to a group annuity purchase as an exit strategy for DB plan sponsors. CDCs are used in Canada, Denmark and the Netherlands.

The company’s pensions team, advised by Willis Towers Watson and Aon, designed the CDC in collaboration with the Communication Workers Union (CWU), advised by First Actuarial. The legislation necessary to make CDCs possible, the Pensions Act 2021, became law earlier this year.

The RSA CDC Pensions Forum was formed earlier this year to support the development of CDC pensions in the UK. The Forum’s sponsors include Aon, First Actuarial, the Institute and Faculty of Actuaries, CMS and Lane Clark Peacock. From TheRSA.org website:

> Collective Defined Contribution (CDC) are a type of pension that allow workers an option of paying into one giant pot with other people from any company they have a pension with. This collective pot is then invested in a way which is designed to provide everyone with an income from the time they retire until the time they die, dependent on how much they have saved.
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> Often workers can only save into an individual pot, and are then left to fend for themselves, not knowing how long they will need their pension savings for. The only current alternative to this is to buy an annuity which is very expensive.

> CDC pensions offer that guarantee. They can make longer term investments and offer economies of scale by pooling the pensions of workers across and between large companies. As a result, they offer much higher pensions than are available by buying annuities.

Royal Mail Group plc, a member of the FTSE 100 Index, is a British multinational postal service and courier company. It was established by King Henry VIII in 1516. Its Royal Mail Group Limited unit operates a letter delivery service (Royal Mail), a parcel delivery service (Parcelforce Worldwide), and a global logistics company (GLS Group).

For most of its history, the Royal Mail was a public service, operating as a government department or public corporation. In 2013, after the Postal Services Act 2011, a majority of the shares in Royal Mail were floated on the London Stock Exchange. The UK government initially retained a 30% stake in Royal Mail, but sold the last of its shares in 2015.

The new pension scheme will be made up of a CDC section and a cash lump sum section (similar to the existing DB cash lump fund, currently worth £1.2bn), with virtually all employees in both. Members will contribute 6%, and the Royal Mail 13.6%, of pensionable pay. Members will accrue 1/80 pensionable pay each year in the CDC section, and 3/80 in the cash fund. The benefits will be a guaranteed minimum lump sum from the cash fund plus a wage in retirement, which will fluctuate depending on investment returns and demographics.

"We won't be using capital buffers to help reduce the unpredictability of income levels, as buffers can place unfair burdens on particular cohorts of members," Gough told IPE. The pension fund's high-level investment strategy, agreed between management and unions, is to target global equity returns with lower volatility.

British national DC plan to allocate 5% of assets to private equity

Defined contribution master trust NEST has decided to allocate 5% of its assets under management (AUM) to private equity—but it won't be following the traditional private equity fee model that involves an annual management charge and carried interest.

"We cannot afford 2 and 20," Mark Fawcett, NEST's CIO, previously told IPE. "We don't think that sort of fee model is value for money for our members."

The publicly sponsored pension plan (AUM £19.4bn, €22.6bn, $26.2bn) is expecting to invest a total of about £80bn in private equity on behalf of its members over the next 20 years. NEST targeted a private equity allocation of £1.5bn ($2.04bn) by the end of 2024.

"We want private equity to play an important role in our portfolio, offering strong returns and diversification," said Stephen O'Neill, NEST's head of private markets. "As ever, we're looking for bidders to present global solutions that will be evergreen and scale with NEST over time," added O'Neill.

Once awarded, the new private equity mandate will be added to the existing range of Retirement Date Funds that make up NEST's default strategy.

The launch of the tender comes after a period of market engagement during which the pension scheme challenged asset managers to come up with a less expensive private equity fee model. A spokeswoman for NEST said that to protect its commercial interests and those of bidders, it could not provide specifics about what fees NEST would accept.

NEST also said that successful fund managers would need to demonstrate that they could offer a robust risk management framework and integration of environmental, social and governance factors into their investment and asset management processes.

NEST has steadily added private market assets in recent years. Its first move into unlisted markets was with private credit, with three mandates awarded in 2019. Since then NEST has also hired managers for direct infrastructure equity investments.