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Experts divided over rally or ruin

Bear Stearns rescue: meltdown marker

With European credit markets having rebounded since March, spreads on corporate bonds easing and risk aversion falling, some commentators have started to ask whether the financial crisis is over. Others, though, have been asking what happens if financial turmoil capsizes the global economy.

Christine Li, Economist at Moody's Economy.com, said the speculative-grade bond market was staging a mini-rally. Since hitting a four-year high of 763 basis points in late March, spreads have narrowed by 165bp and now stand at 604bp above the relevant benchmark securities. This, however, is still high compared with the average 211bp spread during the first half of last year, suggesting that investors remain risk-averse.

Li said that, despite the current unfavourable environment for high-yield borrowers, high-yield spreads were unlikely to widen as much as just before the last credit cycle downturn. In 2001, European high-yield spreads went as high as 1,434bp above the relevant benchmark. She added that borrowing costs were likely to remain strained.

Looking further ahead, an Economist Intelligence Unit (EIU) risk report suggested that the US Fed's rescue of investment bank Bear Stearns elevated the sub-prime mortgage meltdown to historic levels. Financial losses from the US mortgage rout and the spreading credit crunch are likely to approach $1,000bn, according to the IMF.

The EIU report suggested that if the contagion infected ever more assets, the US could plummet into the kind of recession that turned the 1990s into a lost decade for Japan. This would contribute, in turn, to sharp slowdowns globally. In what it called a 30% scenario, the report discussed the possibility of a more dire outcome: a massive, worldwide flight from risk that causes asset values to plunge, banks to collapse, credit to contract and the world economy to stall.

Pensions Regulator's powers beefed up

The government is giving the Pensions Regulator greater powers to require employers to contribute to a pension scheme if their actions threaten the security of members' pensions.

The changes will allow the regulator to reduce the risk to members' interests from scheme changes or corporate transactions. The changes affect employers or their associates, including investors in the employer who might seek to profit from the pension scheme. There will be an eight-week consultation, although most of the changes came in with immediate effect in April.

Mike O'Brien, Minister for Pensions Reform, said: "The Pensions Regulator has done an excellent job in recent years but we need to ensure its powers keep pace with developments.

"Innovation is welcome, but I am concerned that some emerging business models might not give the same protection for pension schemes as traditionally provided by a sponsoring employer or insurance capital. I want to guard against pension schemes simply being treated as a commodity to be bought or sold.

"The most effective way to tackle this problem is to give the regulator the power to require contributions to pension schemes when an employer's actions reduce the security of members' benefits. I want to see pensions secure and promises kept so that members can look forward to a happy retirement."

O'Brien said the powers would only be targeted at risky situations, and that the vast majority of pension schemes would not be affected.

He added: "These measures will also avoid new costs being placed on the Pension Protection Fund, which could ultimately be passed on to responsible employers through the PPF levy.

KEY CHANGES

Contribution notices
Can now be issued to companies that acted in good faith and where there was no intention to impair the position of the scheme as long as there is a detrimental effect (previously intent and bad faith were also required).

Chain rule
Previously, a single identifiable act that caused damage had to be identified, but now the regulator can issue a contribution notice where a number of acts taken together are judged detrimental (with retrospective effect to 2004).

Financial support directions
Can now be attached to groups of entities and persons, rather than individuals, so it is no longer possible to avoid vulnerability to financial support directions by spreading assets around a group.

Bulk transfers
It will not be possible to avoid financial support direction vulnerability by making a bulk transfer to another scheme. This will probably reduce the attraction of certain transition techniques.

"The proposed changes would also allow the regulator to require an employer or associate to make additional contributions to a scheme where a bulk transfer has been carried out and was detrimental to the interests of members."

See www.dwp.gov.uk/pensionsreform/latest_news.asp ■

On the move...

- **Ian Armstrong**, AMCT, has been promoted from Treasury Accountant to Treasury Controller at Rolls-Royce.
- **Conor Maher**, MCT, has appointed Head of International Liquidity at Barclays Bank.
- **Richard Smith**, AMCT, previously at Nestor Healthcare Group, has been appointed Finance Director at Railcare.
- **Peter Williams**, FCT, previously at Cermaq, has been appointed Finance Director at Devro.

MEMBERS' DIRECTORY
Members' contact details are updated regularly at **www.treasurers.org**. *Email changes to Tolu Babatola:* **tbabatola@treasurers.org**, *or phone +44 (0)20 7847 2558.*

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UK businesses feel the crunch

The effects of the credit crunch are increasingly being felt outside the financial services sector, according to a new report.

A recent survey of companies with turnover between £20m and £250m carried out by accounting firm Baker Tilly revealed that a third of respondents had been affected by the credit crunch during the spring.

Nearly two-thirds said that their profits had gone down, and a quarter said that they were finding problems with financing.

Nearly half the respondents were considering cutting costs. The biggest area for potential cost savings was identified as headcount: 25% of companies were looking at limiting recruitment and 15% were considering redundancies.

However, the outlook was not all pessimistic, with 60% of respondents considering listing, and maintaining they would still do so irrespective of the economic situation.

Even so, 64% of companies surveyed said they were implementing risk management controls such as tougher credit controls and assessing customer and supplier risk.

Laurence Longe, Baker Tilly's National Managing Partner, said: "A cross-section of British businesses has begun to feel the widening effects of the credit crunch. Most are considering belt-tightening and are proposing increased vigilance to deal with the tough market conditions."

Pension buyout market to quadruple this year

The market for transferring pension scheme risk from an employer to an insurance company has accelerated sharply over the past six months and is expected to grow rapidly from here.

A pension buyout report from actuarial consultancy Lane Clark & Peacock revealed that at least 10 FTSE 100 pension schemes were evaluating comprehensive quotations to buy out some or all of their pension liabilities during 2008.

Wellsteed: favourable pricing provides a transfer opportunity

The largest buyout transaction completed to date has been an £800m deal to insure current pensioners in the P&O pension scheme, but the report said this milestone might soon be eclipsed. Seven quotations have been issued by insurers for potential transactions over £1bn.

Lane Clark & Peacock predicted that the pension buyout market in 2008 would exceed £10bn – a four-fold increase on 2007 volumes.

The report cited competitive market rates, innovative structures and the ability to partially transfer risk to an insurer without needing to close down the pension scheme altogether as key drivers for companies and trustees pursuing a buyout.

The report said that market growth had been stimulated by the credit crunch, with insurance companies using the higher yields available on investment-grade corporate debt and other assets to reduce their prices.

Clive Wellsteed, who heads the pension buyouts practice at Lane Clark & Peacock, said: "A year ago, many commentators were predicting that the pension buyouts market would be a slow-burner. Now the question is, can insurers keep pace with demand from companies and trustees to offload risk?

"The decision of whether to pass risk to an insurance company through buyout is simply a question of timing. Most defined-benefit pension schemes are closed to new members and were already expecting to buy out with an insurer in the long term. Favourable pricing now provides an opportunity to transfer some or all of the risk away much sooner. It's not a question of whether these schemes will buy out, but a question of when."

See Transferring the Risk, page 26 ■

European money market funds hit new highs

The Institutional Money Market Fund Association (IMMFA) funds under management in Europe have continued to rise to new records.

According to IMMFA, funds in early May exceeded €400bn (£317bn), an increase of 35% over the past year.

The record figure has been achieved during the credit crisis when questions have been raised about the security of some money market funds. IMMFA said its money market funds should not be confused with other money/cash funds.

Other funds are unlikely to be managed with the same principal objectives, but instead seek to provide better returns through longer-dated investments which have more inherent risk or longer settlement periods.

They may also include a wider range of instruments, such as structured products, derivatives, and non-investment-grade securities.

Donald Aiken, Chairman of IMMFA, said: "IMMFA funds continue to grow to new records. Their popularity comes from their ability to deliver on their objectives of capital security and liquidity at all times.

"The combination of being triple-A rated and the ability to provide liquidity and capital security through the challenging market conditions of the last 10 months has contributed to the success of IMMFA funds, especially in this period of prolonged volatility and testing times in the interbank money markets across the globe."

Aiken said that IMMFA had to work with other trade associations and the relevant authorities with a view to defining different sorts of money market funds.

He added that IMMFA money market funds should not be confused with other funds available which can be similarly named. ■

Aiken: IMMFA funds offer security and liquidity