Bank of Ireland

COVID-19 – Impact on Personal Pensions

Frequently Asked Questions

We have witnessed a number of turbulent weeks in investment markets which have had a major impact on the value of personal pension funds. We will set out what it means for personal pension savers, and look at the next steps they might consider.

Investment growth is one of the key contributors to accumulating a pension fund at retirement. However, it is probably the one that varies most – even on a daily basis. It is also the one that has captured a lot of attention in recent weeks. Following the outbreak of COVID-19, stock markets have fallen sharply.

In the past, we have seen sharp falls in share prices on the back of recessions, oil crises, and wars. This time around, the primary drivers have been quite different:

- The cause of the market falls began with a healthcare crisis but attention quickly moved to the economic impact of COVID-19.
- The initial outbreak began in the East but gathered more investor attention as it rapidly infected much of Europe and then to the United States.
- Records were broken as we saw the steepest falls in markets since the 1930's
- Uncertainty remains around the extent at which the Coronavirus would spread.
- Most Global economies have entered recession and economic data has turned extremely negative.
- Markets looking at the implications for the global economy: how can trade cope without a functioning Chinese manufacturing sector?

These negative headlines have been countered by more recent positive news:

- As governments and central banks quickly digested this news, they took substantial steps very quickly – The US government announced a $2 trillion injection into their economy with a probability of more to come. European governments followed suit and along with European Central Bank intervention, major initiatives are now in place to stimulate economic growth. These steps are bigger than anything we have witnessed in the past but they will take some time to take effect.
- At the same time, we have seen a plateauing of new cases and fatalities linked to COVID-19. We watch the data carefully to assess if this is a temporary position or a sustainable trend.
- China was the first country to be hit by the crisis and seems to have taken the necessary steps to emerge from it. All of the data suggests that China, the "World's manufacturer" is getting back to work which should help to re-establish supply chains.

Stock markets have responded in a very positive manner. We have seen some sharp rebounds across the World but volatility remains a feature. We are not out of the woods yet and we may see some testing of lows in the months ahead. We are taking some confidence from the fact that the conditions we needed to see for recovery are starting to take hold.

Will this impact those with personal pensions?

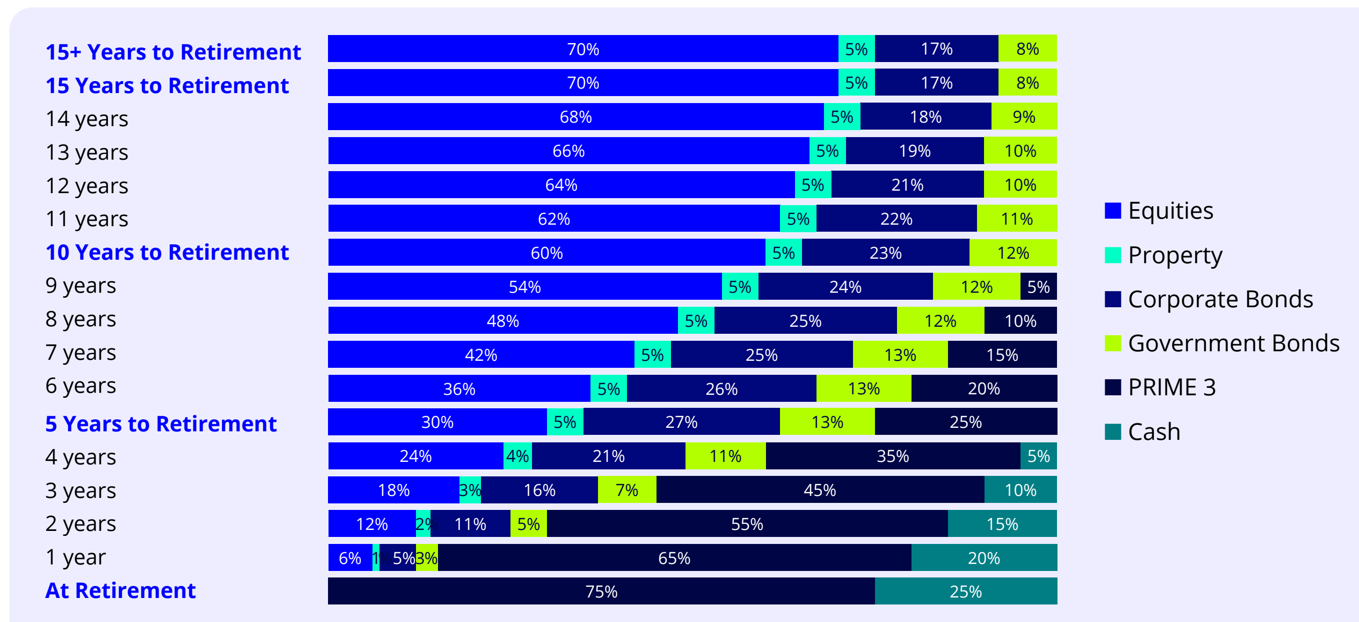
It is important to remember that one size does not fit all: we offer customers a broad choice of investment funds, so not every employee chooses to invest in the same way. You can choose from more than 50 different investments funds ranging from very low risk to very high risk. These include; options that invest in shares, those that invest in bonds, and others that spread your money across a range of different asset classes. The impact of the recent falls on your pension fund depends on how your retirement savings are invested.

The Fund Centre is a useful resource which allows you to understand how your money is invested and how your funds have performed. You can access it by clicking here.

The funds in either low to medium risk, medium risk, and medium to high risk did not suffer the full brunt of stock market sell-offs. This is because they are diversified across other assets, including bonds, property and cash. This means that while shares fell sharply, other investments delivered positive returns.

Many of our personal pension holders choose two funds from those available, namely Passive IRIS and IRIS. These use what is known as a Lifestyle Strategy. The idea here is that if you have a long way to go to retirement, you want to maximise growth in your savings. You do this by investing in what we call real assets which are typically shares and property. As we saw recently, shares can, and do, go up and down in value, but we know that, over the long term, they generate the best returns for investors. However, as you near your intended retirement age, you may want to consolidate gains and limit the ups and downs. We achieve this by automatically switching your holdings gradually into more conservative assets such as bonds and cash, generally from about fifteen years from your retirement date.

The chart below shows you how Passive IRIS operates this strategy:



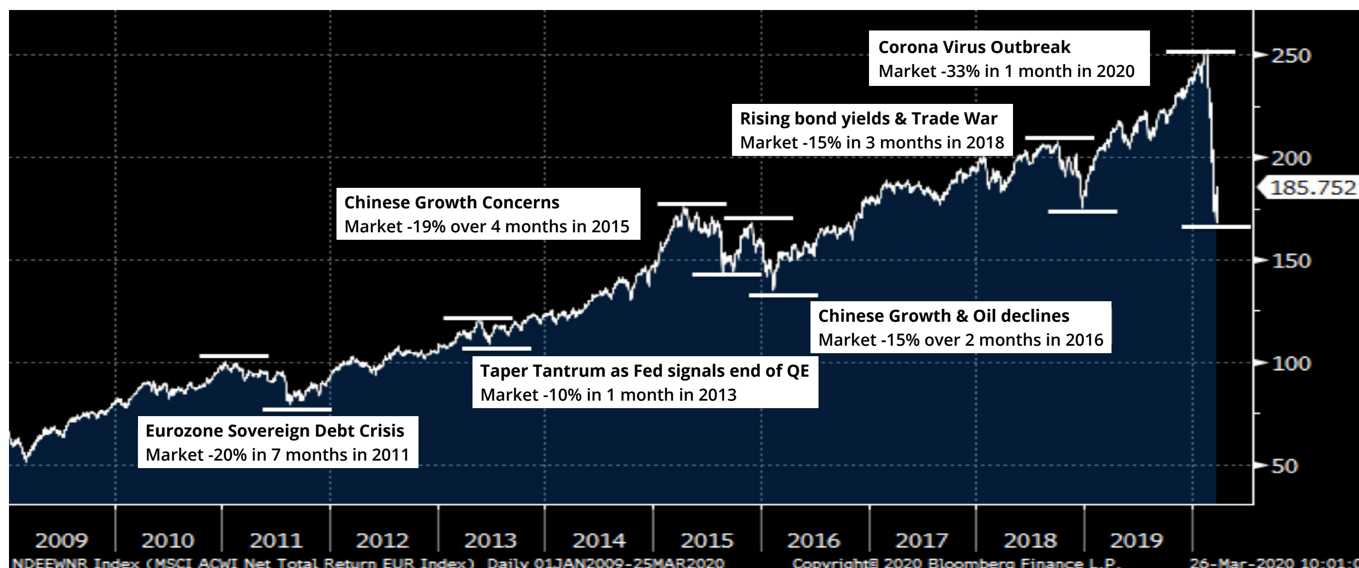
Because of their higher stock market content, IRIS/Passive IRIS investors that still have a long way to go to retirement saw a greater fall in the value of their funds, than those who are closer to their retirement date. The funds available to you manage money in many different ways, and their allocation to different assets can change to reflect changing investment conditions, like we're experiencing now. Under the bonnet of a number of these funds, we have seen some changes that have limited the impact of market sell-offs. A number of our PRIME Funds have heavily reduced their stock market exposure in recent weeks. iFunds 3, 4, and 5 have increased allocations to government bonds. Changes such as these can cushion your pension fund from some of the recent falls.

Your Individual Personal Pension

The key thing to remember is that your pension fund should be as individual as you are and should be invested accordingly. It should reflect your attitude to risk, your expected retirement date, and you should contribute the optimal amount to achieve your goals.

Longer Term Context

It is important that we remember that the funds referred to above are intended as vehicles to help you save for an event in the future, i.e. your retirement date. For most readers, this date may be many years from now. Up to the point that markets began to sell off in February, we had seen many stock exchanges announcing that they had reached all-time record highs. If we look back over the last decade, investors have been well rewarded, albeit with many speed bumps along the way. The chart below shows world stock market performance since 2009. The recent falls certainly feature but we have seen plenty of other setbacks, notably in 2011, 2015 and 2018. However, in most cases the recovery has come quite quickly.

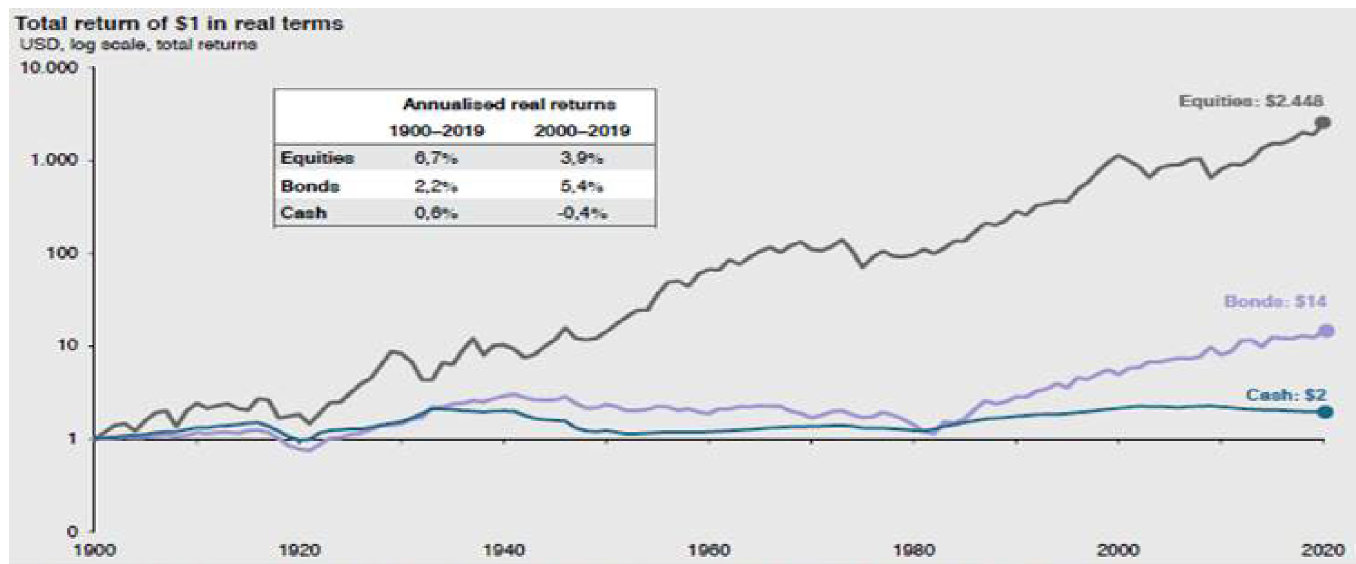


WARNING: Past performance is not a reliable guide to future performance.

For those that remain patient we know that over the long term, investing in shares has delivered better returns than other asset classes. Historically, you can see that stock markets have rebounded sharply from these falls.

What is the best home for my personal pension savings?

The chart below shows the returns from investing just €1 in shares, bonds and cash, after inflation as far back as 1900. The stock market has been the clear winner. If we just look at the last decade which includes two of the biggest crashes – the Dot Com bubble collapse of 2001-2003 and the Great Financial Crisis in 2008 and 2009, bonds proved to be a better home for your money. Again, this is why we recommend that customers diversify across these asset classes. To answer the question, generally, you are better served by having a mix of shares, bonds, property, cash and alternatives.



Annualised real returns	1900–2019	2000–2019
Equities	6,7%	3,9%
Bonds	2,2%	5,4%
Cash	0,6%	-0,4%

Source: Bloomberg, Bloomberg Barclays, FactSet, Shiller, Siegel, Standard & Poor's, J.P. Morgan Asset Management. Pre 2010 returns: Shiller, Siegel; from 2010: Equities: S&P 500; Bonds: Bloomberg Barclays US Treasury 20+ year Total Return Index; Cash: Bloomberg Barclays US Treasury Bills Total Return Index. Past performance is not a reliable indicator of current and future results. *Guide to the Markets - Europe*. Data as of 31 December 2019.

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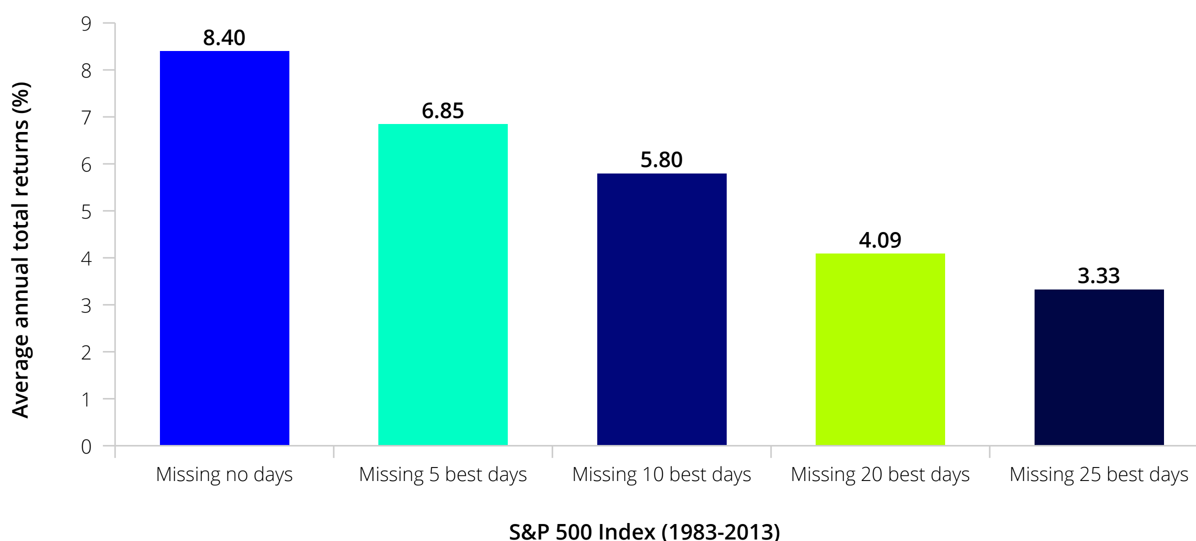
One of the other key lessons for personal pension holders is to allow your investment time to do what it's meant to do – deliver long term growth. Unfortunately, many investors take fright when markets fall and jump to the asset that they see as safest – cash. The thesis generally is to get out when others are also getting out ("the herd mentality") and to time things just right to get back in when markets turn around and start to resurge. The folly here generally lies in the second part of the equation – most people miss the rebound and usually only get back in when the strongest recovery has already taken hold. Many need the comfort of a rebound that sustains over time, before they are ready to re-enter the market.

The chart below shows us clear examples of this in action. The investor who stays the term achieved a very healthy return of 8.4% p.a. with plenty of ups and downs along the way. However, if this person misses the best 5 days, their return falls to 6.85% p.a. The one who missed the best 25 days saw a huge drop to 3.3% p.a. When we refer to "best days", we are usually looking at the strongest rebounds that occur generally after a sharp market sell-off. If we translate this into monetary returns instead of percentages, on a notional investment of $50k, we see a return of c. $562k for missing zero days compared with a return of c. $125k for missing 25 days.

Remember, it is time invested in the market, not market timing



Source: Columbia Management Investment Advisors, LLC, Ned Davis Research, Inc., 12/31/83-12/31/13.

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Primary Considerations for Pension Savers Today

Why has the value of my pension fund fallen and why did it happen so quickly?

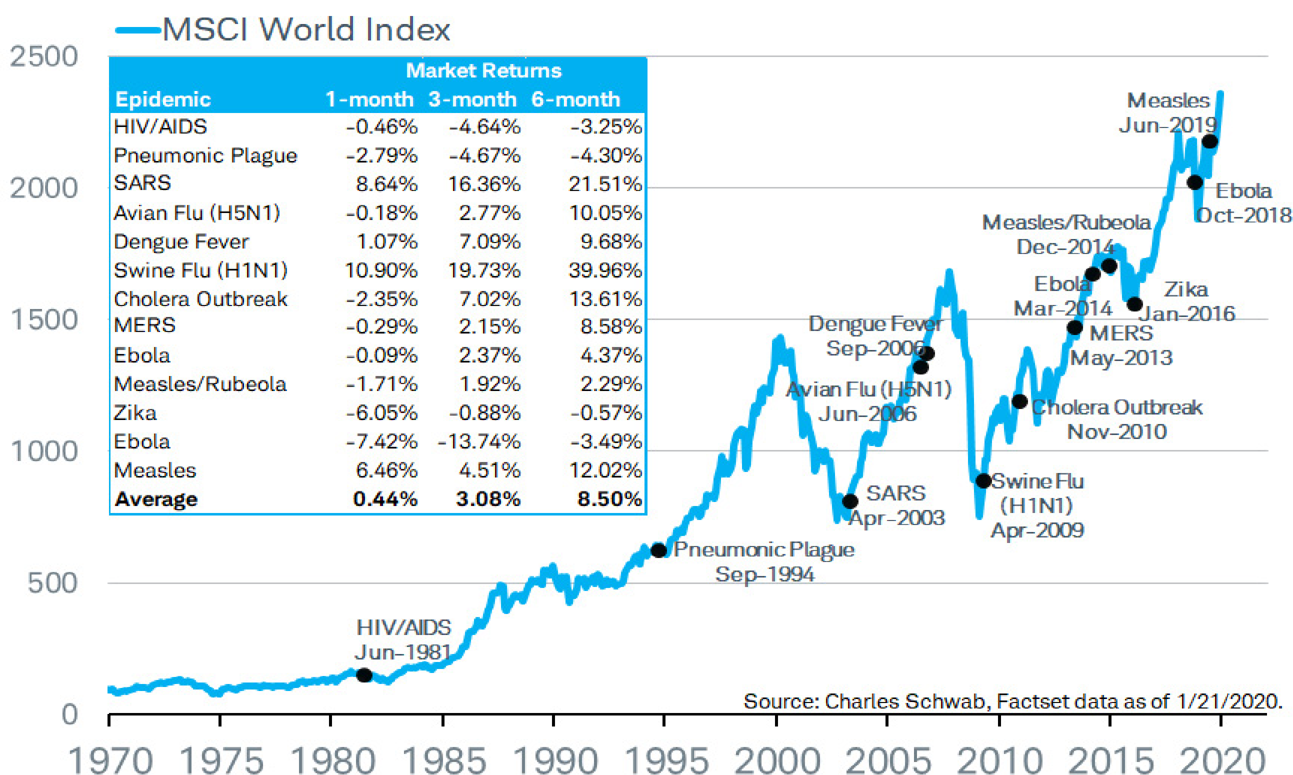
The fall in markets was caused by the outbreak of the Coronavirus and uncertainty about how quickly it would spread across the world. Investors are worried about the impact that inevitable cuts in production, manufacturing, commerce, and trade will have on economies. It is inevitable that we will see this news negatively impacting company profitability and balance sheets. Any decline in company fortunes leads to job losses which would lead to a drop in consumer confidence and consequently to reduced spending.

Is this 2008/09 all over again?

We do not believe this is the case because we do not believe that we were investing in a major speculative bubble like we had witnessed in 2008/09. Furthermore, the banking sector has been recapitalised over the last decade and is in a far better condition to withstand a major correction. Interest rates and inflation are all at very low levels.

When will we see markets stop falling and when will they recover?

This two-part question is more difficult to answer this time than in the past for a number of reasons. In the past, we saw how world stock markets responded to health scares such as AIDS, H1N1 and Ebola. (see chart below) In most cases, a sharp sell-off was followed by a sustained recovery.



Epidemic	Market Returns 1-month	3-month	6-month
HIV/AIDS	-0.46%	-4.64%	-3.25%
Pneumonic Plague	-2.79%	-4.67%	-4.30%
SARS	8.64%	16.36%	21.51%
Avian Flu (H5N1)	-0.18%	2.77%	10.05%
Dengue Fever	1.07%	7.09%	9.68%
Swine Flu (H1N1)	10.90%	19.73%	39.96%
Cholera Outbreak	-2.35%	7.02%	13.61%
MERS	-0.29%	2.15%	8.58%
Ebola	-0.09%	2.37%	4.37%
Measles/Rubeola	-1.71%	1.92%	2.29%
Zika	-6.05%	-0.88%	-0.57%
Ebola	-7.42%	-13.74%	-3.49%
Measles	6.46%	4.51%	12.02%
Average	**0.44%**	**3.08%**	**8.50%**

The MSCI World Index captures large and mid cap representation across 23 Developed Markets countries. With 1,646 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. **Past performance is no guarantee of future results.**

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COVID-19 may prove to have more catastrophic consequences than other health scares that we have seen in recent years. It will take some time for the world to digest its full implications. This time, it is much harder to predict the timing and shape of a recovery. The speed and extent of sell-offs and dearth of buyers suggests to us that a "V-shaped" stock market rebound is very unlikely. The level of economic disruption is likely to be so extensive that it will inevitably lead to weaker corporate earnings, thus weakening balance sheets. It is difficult to see how a global recession can be avoided in response to these events. We have moved our mind set from suggesting a possible to a highly probable short lived recession.

We cannot discount the likelihood that stock markets are likely to remain volatile for an extended period of time and it may take some time before we see a sustained recovery. However, if you are saving on a regular basis, you may benefit from buying cheaper assets which should see higher valuations in time.

Should I switch to cash?

To answer this question, we need to go back to the core investing pillars:

1. Has your attitude to risk changed from when you originally invested?
2. Have your investment goals changed? i.e. is growth still a priority for you?
3. Has your investment horizon changed?

When you originally took out your personal pension, your goal was probably to accumulate a decent pension fund for retirement. As we saw earlier, investment growth is one of the key ingredients in the strategy to achieve your goal. Investing in shares and property is how most participants in personal pensions realize that growth. If you move your funds to cash, you are minimising your chances of further losses but unless you successfully re-enter the market just before it starts to grow again, you will miss out on the recovery. Buyers and sellers have re-rated their views of shares to reflect an unprecedented crisis. The value of your assets has now been marked down to reflect these lower valuations for the present.

If your answer to the questions above has changed and, in particular, if you have a short to medium term imperative to access your pension, you should meet with an advisor to reassess your goals and the priorities for your retirement plan.

We believe that this is a time when patience is likely to be rewarded but that it may take some time for this scenario to play out. The fundamentals of long-term investing remain unchanged:

- Allocate your money to a high quality, well-diversified portfolio of assets.
- Ensure you have an adequate level of real assets such as shares and property to deliver growth
- Allow time, the most important ingredient in the investment mix, to play its part.

As always, in times like this, getting the right information to make informed decisions is important to determine the right investment strategy.

If you have any queries, please don't hesitate to contact your Wealth Manager or email us at info@bankofirelandlife.ie

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