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Consultants and Actuaries

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Topic to be covered:

Volatility in the Interest Rate – March 2020

Contents:

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Background

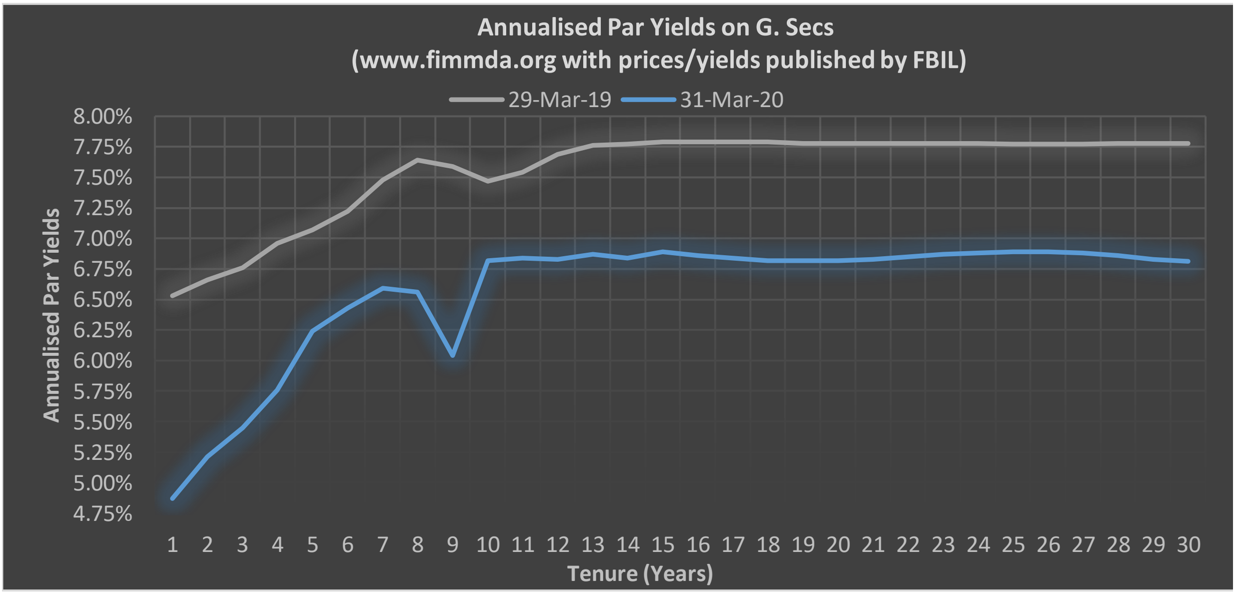
- Employee Benefit Obligations are to be valued based on G-Sec rate of estimated term of obligation (expected future service/ expected future lifetime) as prevalent at the end of the reporting period.
- 10 Years G.Sec. Yield was 7.47% as on 29th March 2019 and is 6.82% as on 31st March 2020, resulting in decrease in the yield of 0.65%.
- CPI Index:

Jan 2020 - Dec 2019	0.00 %	Jan 2020 - Jan 2019	7.49 %
August 2019 - July 2019	0.31 %	August 2019 - August 2018	6.31 %
March 2019 - Feb 2019	0.65 %	March 2019 - March 2018	7.67 %

- The yearly CPI has slightly decreased from 7.67% in March 2019 to 7.49% in January 2020.
- Impact of change in assumption is recognised in Profit & Loss in case of AS 15, whereas in case of Ind AS 19 it is recognised though OCI (post-employment obligations).
- As Discount rate has decreased it will result in an increase in liability and Actuarial loss on obligation due to change in financial assumptions.

Changes

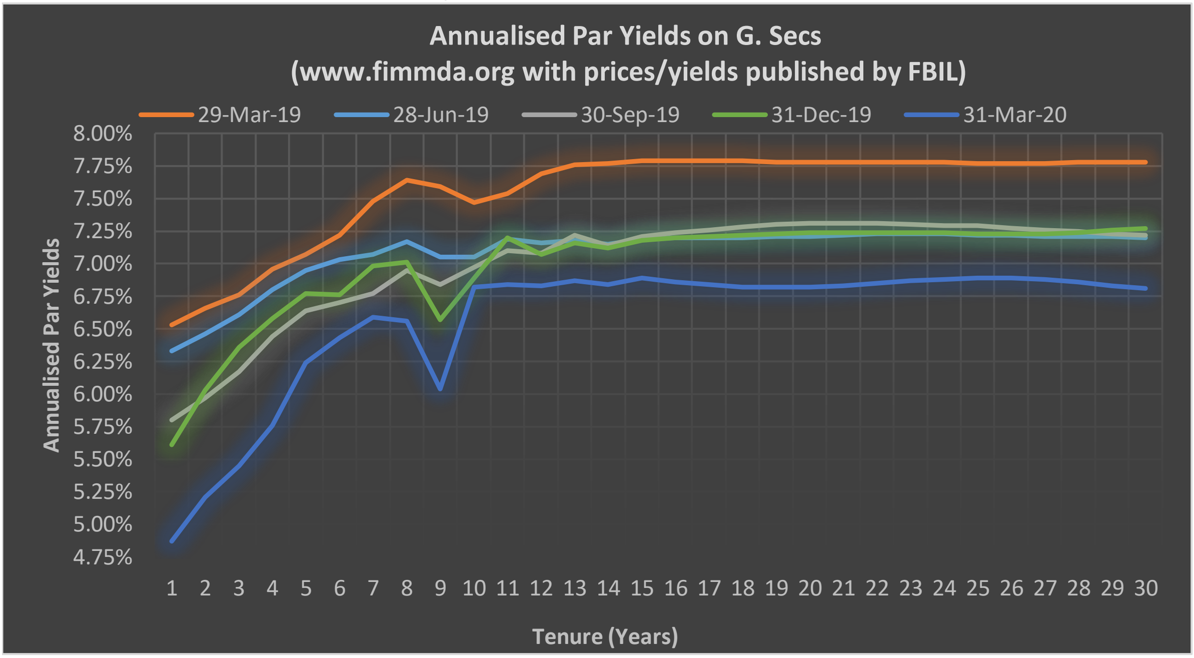
Below is chart of G - Sec rates at March 2019 and March 2020:



Annualised Par Yields on G. Secs as at 31-03-2020 (www.fimmda.org with prices/yields published by FBIL)

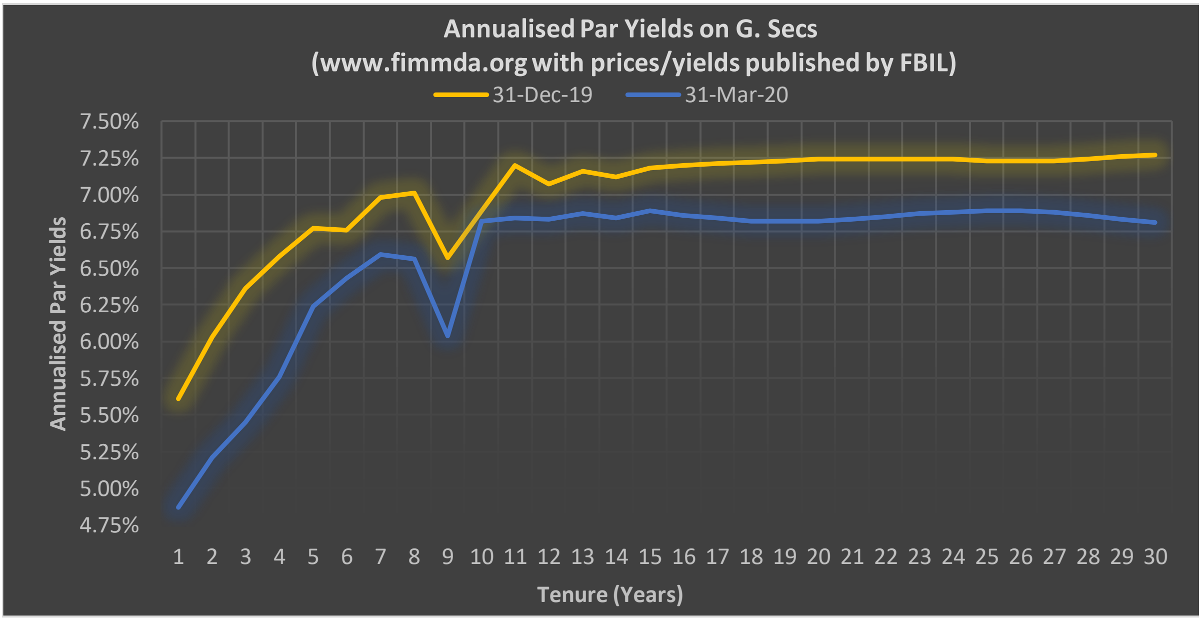
Tenure	1	2	3	4	5	6	7	8	9	10
Yield	4.87%	5.21%	5.45%	5.76%	6.24%	6.43%	6.59%	6.56%	6.04%	6.82%
Tenure	11	12	13	14	15	16	17	18	19	20
Yield	6.84%	6.83%	6.87%	6.84%	6.89%	6.86%	6.84%	6.82%	6.82%	6.82%
Tenure	21	22	23	24	25	26	27	28	29	30
Yield	6.83%	6.85%	6.87%	6.88%	6.89%	6.89%	6.88%	6.86%	6.83%	6.81%

Below is comparison of quarterly G - Sec rates of 2019-20:



- As compared to March 2019, G-Sec rate has reduced by approximately 100 basis points at the end of March 2020.
- For short to medium term bonds upto term of 4 years, the discount rate has reduced significantly by approximately 140 basis points.
- G-Sec rate for term of 9 years has decreased significantly as compared to March 2020.

Below is comparison of G - Sec rates of December 2019 v/s March 2020:



- As compared to December 2019, G-Sec rate has reduced by approximately 40 basis points at the end of March 2020 except in case of 10 years bond where it has decreased by only 7 basis points.
- For short to medium term bonds upto term of 4 years, the discount rate has reduced significantly by approximately 80 basis points. This is majorly due to Covid-19 and recent RBI rate cut.

Comments

- Decrease in G- Sec yield will increase the Actuarial liability.
- In case Ind AS valuation is taken by company, Expense in OCI due to the change in discount rate assumption can be estimated from Sensitivity of Obligation as disclosed at March 2019 under Ind AS 19.
- If a correlation in the assumptions are to be considered, one must take a re-look at the future salary escalation and if the net gap remains same, there may not be much change in the liability. One must discuss this correlation with actuaries and auditors.
- There is also a possibility of the fair value of the plan assets going upward due to the decrease in the yield which may result in offsetting some the of the impact of lower discount rates. This will only impact funds where assets are measured on a mark to market basis.
- G-Sec rate is very volatile and decreased to significantly low rate in past 2 years, this resulted in Actuarial Losses on Define Benefit Obligations in 2018-19. In the current 2019-20, we will see this again, unless other assumptions are updated to offset the discount rate impact. Changing other assumptions should be done after careful consideration and in discussion with your actuary and auditor.
- In the case of Ind AS this volatility is passed through OCI for Post-Employment Benefit plans so the Profit and Loss account will remain consistent.
- Discount rate is taken based on G-Sec rate of estimated term of obligation. Estimated term of obligation is calculated by actuarial techniques applying probability of attrition and mortality rates.
- Discount rate is based on market yields i.e. deal rates at the end of the reporting period on traded government bonds. This is annualised par yield for respective term of bond.

Reference:

Inflation: http://www.inflation.eu/inflation-rates/india/current-cpi-inflation-india.aspx
G-Sec Yield: (www.fimmda.org with prices/yields published by FBIL) (Per Annum yield)

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