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Consultants and Actuaries

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Topic to be covered:

Volatility in the Interest Rate - September 2019

Contents:

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Background

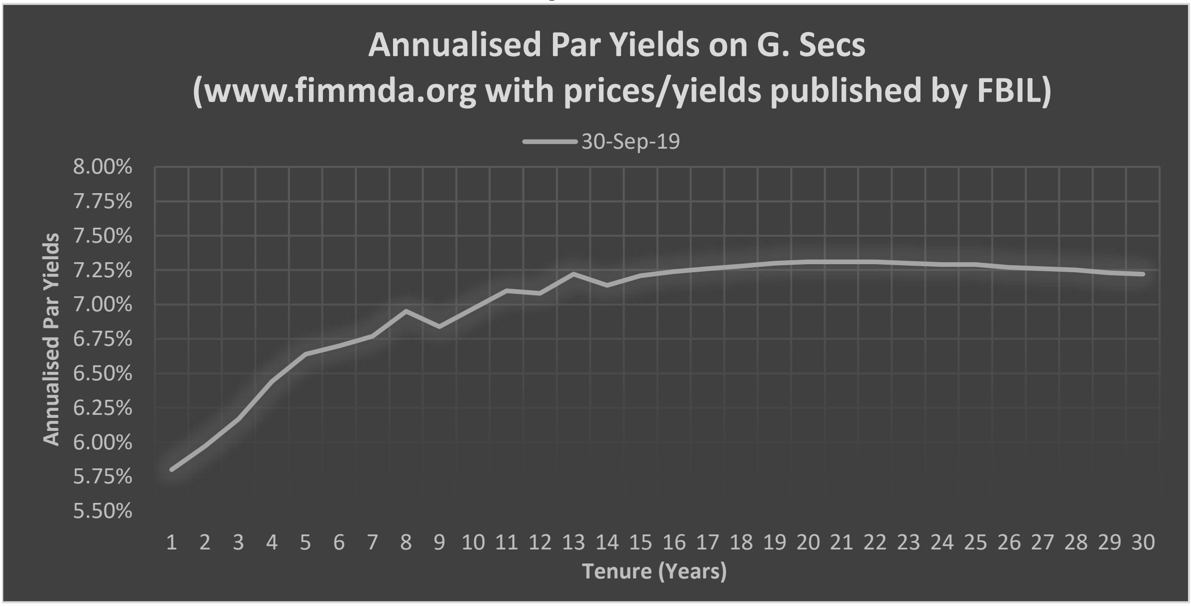
- Employee Benefit Obligations are to be valued based on G-Sec rate of estimated term (expected future service/ expected future life time) as prevalent at the end of the reporting period.
- 10 Years G.Sec. Yield was 7.47% as on 29th March 2019 and is 6.97% as on 30th September 2019, resulting in an increase in the yield of 0.50%.
- CPI Index:

August 2019 - July 2019	0.31 %	August 2019 - August 2018	6.31 %
July 2019 - June 2019	0.95 %	July 2019 - July 2018	5.98 %
March 2019 - Feb 2019	0.65 %	March 2019 - March 2018	7.67 %

- The yearly CPI has decreased from 7.67% in March 2019 to 6.31% in August 2019.
- 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 into increase in liability and Actuarial loss on obligation due to change in financial assumptions.

Changes

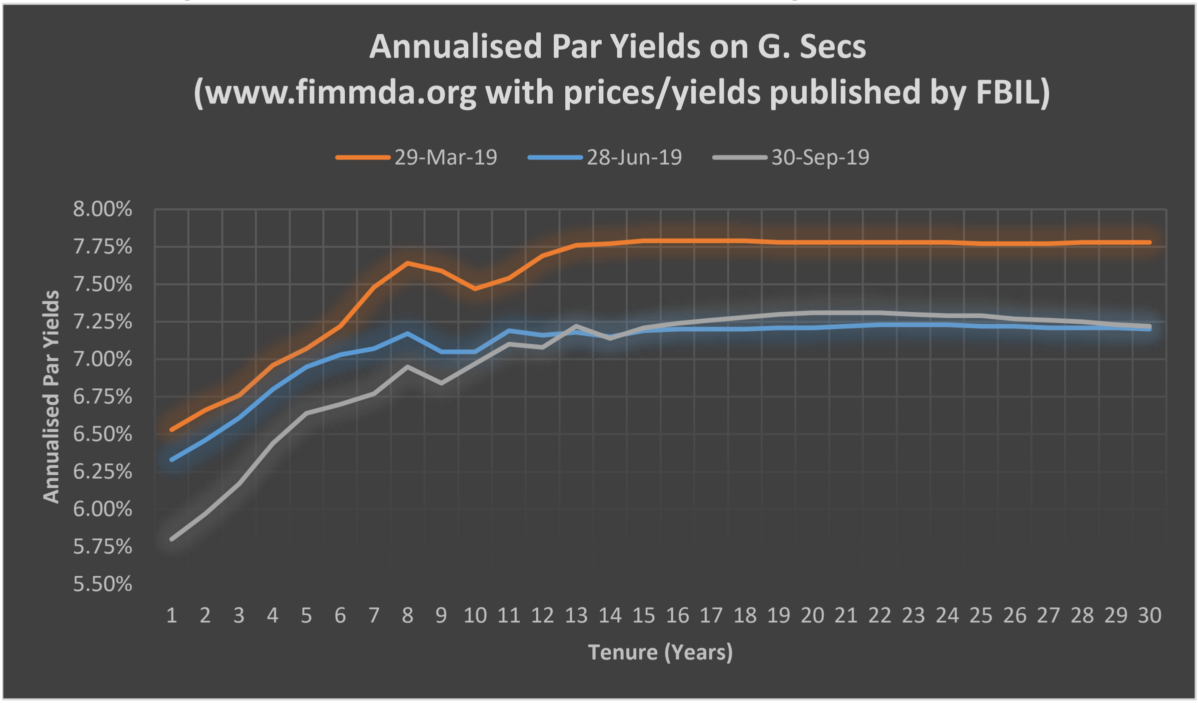
Below is chart of G - Sec rates at 30th September 2019:



Annualised Par Yields on G. Secs as at 30-09-2019 (www.fimmda.org with prices/yields published by FBIL)

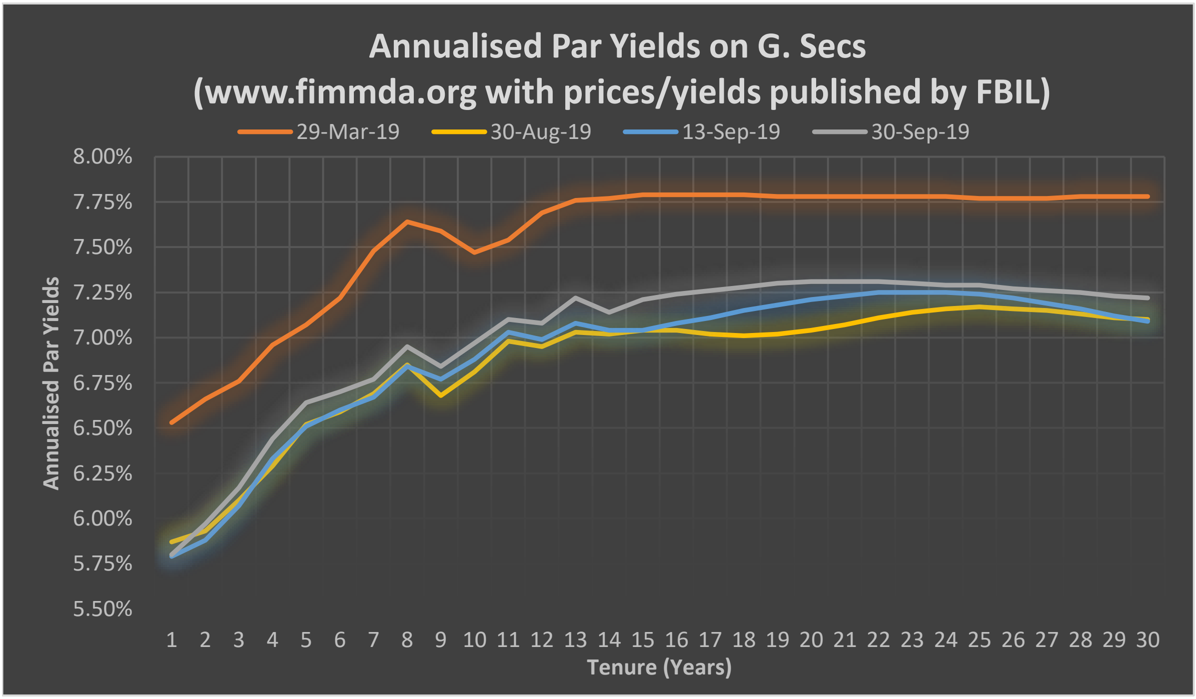
Year	1	2	3	4	5	6	7	8	9	10
Yield	5.80%	5.97%	6.17%	6.44%	6.64%	6.70%	6.77%	6.95%	6.84%	6.97%
Year	11	12	13	14	15	16	17	18	19	20
Yield	7.10%	7.08%	7.22%	7.14%	7.21%	7.24%	7.26%	7.28%	7.30%	7.31%
Year	21	22	23	24	25	26	27	28	29	30
Yield	7.31%	7.31%	7.30%	7.29%	7.29%	7.27%	7.26%	7.25%	7.23%	7.22%

Below is comparison of G - Sec rates of March – June - September 2019:



- For term of 15 years or more G-Sec rate has increased slightly as compare to June 2019.
- For short term to medium term bonds, G-Sec rate is lower which may result into actuarial loss on obligation.

Below is comparison of G - Sec rates during last 1-month v/s March 2019:



- G – Sec rate has reduced significantly post March 2019.
- Post August 2019 it has started to increase, and it can be observed that gap of G-Sec rate as compare to March has reduced.

Comments

- Decrease in G- Sec yield will increase the Actuarial liability.
- In case Ind AS valuation is taken by company, Income 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 to have correlated assumptions.
- There is also a possibility of the fair value of the Plan Assets going upward due to the decrease in the yield resulting in the lower provision requirements for funded plans which are linked to market movement.
- G-Sec rate is very volatile and decreased to significantly low rate in past, this had resulted into Actuarial Loss on Obligation in 2018-19. In this period, since discount rate has decreased further significantly post March 2019, it will lead to *Actuarial Loss on Obligation due to change in financial assumption*.
- In case of Ind AS this volatility is passed through OCI for Post-Employment Benefit plans so Profit and Loss account remain consistent.
- Discount rate is taken based on G-Sec rate of estimated term of obligation, as G-Sec rates vary a lot across various term of bonds. Estimated term of obligation is calculated by actuarial techniques applying probability of Attrition and death rate. So, it is suggested to review Attrition rate assumption based on actual experience and future outlook of company.

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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