

Dear APS member,

The Airways Pension Scheme – Actuarial valuation up-date

In our last edition of In Focus I said I hoped to be able to write again in the Autumn with the final actuarial valuation results. There are a number of regulatory and documentary formalities that need to be completed before we are able to issue the Actuary's report and the new Statement of Funding Principles, however, I am pleased to be able to write to you with confirmation that agreement has been reached that allows us to conclude the valuation process.

As you will have seen from our previous communications, during the last three years we have improved the long-term security of APS by reducing our holding of equities (shares) in favour of less risky bonds. This actuarial valuation has provided another opportunity to further improve the security of your benefits in the Scheme.

Since the last valuation in 2003, the Pensions Act 2004 has changed the manner in which valuations are carried out. The Trustees now have greater responsibility and it is they, in agreement with the Company, who must agree the different financial and other assumptions used in the valuation process (such as future life expectancy). We have worked closely with, and taken advice from, our Actuary and our other advisors to ensure we have understood all of the factors surrounding those assumptions.

The Pensions Act 2004 also requires the Trustees to understand the on-going financial strength of British Airways. To help us in this work, in conjunction with the trustees of the New Airways Pension Scheme, we employed PricewaterhouseCooper (PwC), the largest creditor advisory firm in the world.

Overall, the advice we have received has helped us come to the following key conclusions:

- As we have reduced the equity holdings to better match the liabilities, we expect our investment returns in the long term to be lower than had been assumed in 2003. This lower investment return expectation also reflects the current low interest rate environment and observed market trends with reduced bond yields and reduced dividend growth. Taken together, our expectation of future returns (known as the discount rate) has been lowered from 5.4% pa in 2003 to 4.5% pa. If actual returns exceed these expectations, the additional funding will provide further benefit security.
- Because of improvements in life expectancy for APS members and pensioners, we know we will need to pay pensions for longer. For example a member aged 60 now, can be assumed to live 2.2 years longer than a member who was 60 in 2003. This adds extra costs to the Scheme.
- Despite changes to the investment and life expectancy assumptions increasing the value of the liabilities, APS remains broadly in balance. In fact there is a small surplus, albeit lower than in 2003; however, there is no Disposable Surplus.

- As the Scheme retains a small surplus British Airways does not need to pay any deficit contribution in respect of pensions already built up. Nonetheless, the Trustees have used their enhanced role under the Pensions Act to negotiate with the Company that it will provide APS with a guarantee from a bank (known as a Letter of Credit) to the value of £230 million. This provides additional security to the Scheme and is a guarantee that the Trustees would be able to rely upon under certain circumstances (for example, if British Airways were to become insolvent).
- We have agreed that the Company will continue to pay on-going contributions in respect of active members at a rate of around £25 million a year.

Taken together, we believe that this package of measures ensures that APS not only remains well funded but is much more secure against future risks. If British Airways were to become insolvent and unable to make further contributions, the Scheme would receive a significant payment from the Letter of Credit, thereby increasing the likelihood of being able to pay all benefits as they fell due.

In closing I want to take the opportunity to stress that the press comment you may have seen in respect of British Airways and its pension arrangements does not affect your Scheme. The benefit reduction proposals put forward by the Company are in respect of the New Airways Pensions Scheme which is in deficit and is entirely separate from your pension scheme arrangements.

We will write to you again in the New Year once we have completed all the remaining tasks associated with the valuation but in the meantime, on behalf of all the Trustees, I wish you the compliments of the season.

Yours sincerely,

Roger Maynard
Chairman of the Trustees of APS