

Summary Annual Report 2016



Foreword

The 2016 financial year saw a dramatic start. A funding ratio of 89.2% at the end of February gave PME every reason to gear up for a cut in pensions. A slowly improving trend began in the following months, however, and at year-end PME recorded a funding ratio of 96.2%, close to its year-earlier level. There was thankfully no question of curtailing pensions.

Fragile situation

Our current position remains nevertheless fragile. We are required to raise our funding ratio to at least 104.3% by year-end 2019. Failure to do so would mean we had fallen short of that minimum for five years on end, and would face a regulatory requirement to cut pension levels. We thus have three years to restore our funding position. Our 10.3% return on investment in 2016 is heartening. In the present low interest rate environment, however, that is not yet sufficient to compensate for the extra provisions needed for our current and future pension liabilities. Another factor is that a funding ratio still below 100% will be under growing pressure through payouts of existing pension entitlements. That puts a brake on recovery and increases the risk of a cutback in benefit levels.

Our current contribution level is moreover inadequate relative to our pension liabilities. Contribution levels were fixed under a five-year agreement in the pension contract between social partners in the Metalektro industry. With interest rates persistently lower than predicted the agreed contribution level is not expected to be adequate throughout that full term. We have shared our concerns on this point with the social partners.

Mutual advantages

In 2016 we continued to seek ways to exploit the partnership between the two metal industry pension funds PME and PMT by utilizing advantages of scale. Measures adopted included the closure of the Radarpoort office of our administrator MN in Amsterdam, and the company has meanwhile relocated all its activities for PME and PMT to The Hague. The MN payroll shrank substantially in 2016. But relocation and reorganisation have had no impact on MN's service level and quality of its pension administration. The board wishes to express its gratitude to the staff of MN in this respect.

In 2016 it became clear that the actual costs incurred by MN exceeded the fees it charged to PME. This gave rise to a fresh agreement between PME and MN on cost-effective fee rates. Pension administration costs will be higher in 2017 as a result. PME finds this increase acceptable from a strategic business partnership perspective. The new arrangement includes agreements on lowering fees in due course and improving the quality of service provision. We are in close consultation with MN on the potential to organise pension administration more efficiently and reduce costs. PME believes MN has not been successful enough in utilizing advantages of scale and controlling costs since it took on the fund's pension administration in 2010.

PME is furthermore confronted with VAT charges to which not all large pension funds are subject. That has led us into a struggle to avoid having to pay VAT over both pension administration and asset management. These efforts add further to our administration costs. Together with the Pension Federation (Pensioenfederatie) and other pension funds we have set up an offensive campaigning for equal treatment of all pension funds. There are inequalities under the current VAT regime that unjustifiably discriminate against some groups or participants.



Departure of board members

On 15 October 2016 Mariëtte Simons stepped down as executive director for pension policy and communication. Since her appointment to that position in August 2014 Mariëtte has made a significant contribution to organising and giving shape to the reverse mixed management model that was launched on 1 July 2014.

In 2016 we also saw the departure of two invaluable non-executive board members on grounds of our envisaged shrinking of the non-executive board: Jos Brocken (employee representative) and Ruud de Charro (employer representative). Both representatives have been keenly dedicated to their work as board members. Jos had been an active board member for the previous 10 years. His work for the fund was of particular significance during the years of financial crisis. We are highly appreciative of the dedication shown to PME by both men during their term of office.

On 31 March 2017 we learned the sad news that Ruud de Charro had passed away. Geert Lathouwers, member of the accountability council, died shortly afterwards on 7 April 2017. We are deeply saddened by their loss.

Future prospects

PME is convinced that participants in a collective pension scheme based on joint and several solidarity are better off than they would be with other schemes based on individual liability. This conviction underlies our regular consultations with other large pension funds and our talks within the Pension Federation (Pensioenfederatie) on developments relating to the pension system as a whole. We look forward with keen interest to decisions to be taken on the future of the system by the new cabinet in The Hague, and thereafter to decisions by the social partners on how these will be implemented in the Metalektro industry. We hope for simplicity, enabling the system to be administered at low cost and in a manner that is lucid to our participants.

The Hague, 15th June 2017.

On behalf of the PME Management Board,

Franswillem Briët
Chairman



Financial position

Policy funding ratio

The funding ratio is the financial barometer of a pension fund. It is the ratio between the fund's available pension assets and its liabilities. Liabilities are defined as the value of the accrued pensions the fund is committed to pay currently and in future (pension liabilities provision). This figure is calculated at a rate of interest prescribed by the Netherlands central bank DNB (De Nederlandsche Bank).

The funding ratio is specified in Figure 1, which shows both the funding ratio (at reference date) and the policy funding ratio (average funding ratio over the previous 12 months). The policy funding ratio is the factor that determines whether a pension fund has a funding shortfall. The (current) funding ratio is significant for policy on investment and interest rate hedging.

• Figure 1: Breakdown of PME's funding ratio

(Amount x € 1 million)	31-12-2016	31-12-2015
Total assets	46,453	42,557
Liabilities and other amounts payable	(1,714)	(1,869)
	<hr/> 44,739	<hr/> 40,688
Other purpose provisions (conditional supplemental pension)	(105)	(79)
Premium equalisation account	(132)	(112)
	<hr/> 44,502	<hr/> 40,497
Available assets	44,502	40,497
Pension liabilities provision	46,281	42,127
Funding ratio	96.2%	96.1%
Policy funding ratio	91.8%	97.6%

At year-end 2016 the policy funding ratio stood at 91.8% (end 2015: 97.6%). That percentage fell short of the regulatory minimum requirement of 104.3%. PME consequently has a funding shortfall and is obliged to draw up a recovery plan. The recovery plan sets out how PME expects to improve its financial position in the years ahead to ensure that it has enough resources in due course to cover its prospective pension benefit commitments and reaches the required minimum ratio (2016: 120.1%). The plan provides for PME to complete its recovery within the mandatory 10-year limit, which means there is no need to curtail pension levels.



Real funding ratio

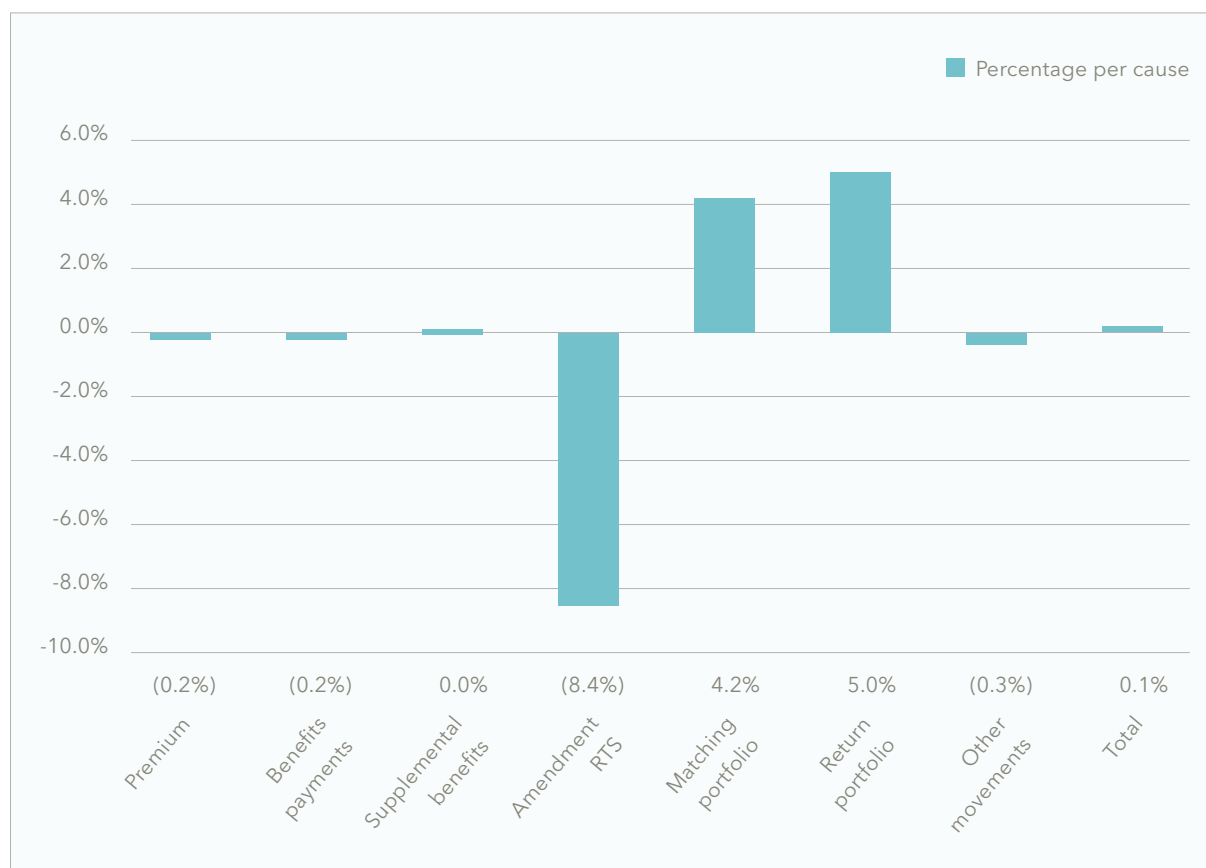
Under the new Financial Assessment Framework nFTK (Financieel Toetsingskader), pension funds are required to report a real funding ratio as well as a policy funding ratio as referred to above. This requirement also applies to the methodology for determining that ratio. A real funding ratio indicates whether a pension fund is in a position to raise pension levels in line with the consumer price index. A real funding ratio of 100% means a fund has sufficient cash reserves to raise nominal pension levels by the conditional price index. At year-end 2016 PME's real funding ratio stood at 75.2% (2015: 79.3%). The drop in the real funding ratio reflects the decline in the policy funding ratio over the year.

Movement in funding ratio in 2016

The funding ratio rose marginally in 2016 from 96.1% to 96.2%. That is an increase of just 0.1 percentage point. The underlying causes of this movement are shown in Figure 2 below.

The most significant factors impacting on the funding ratio in 2016 were the amendment of the nominal interest rate for pension liabilities (interest rate term structure RTS) and yields on the return portfolio and matching portfolio. Although these factors, when taken separately, each had a relatively strong impact, their combined impact on the funding ratio remained marginal.

• Figure 2: Causes of movement in funding ratio

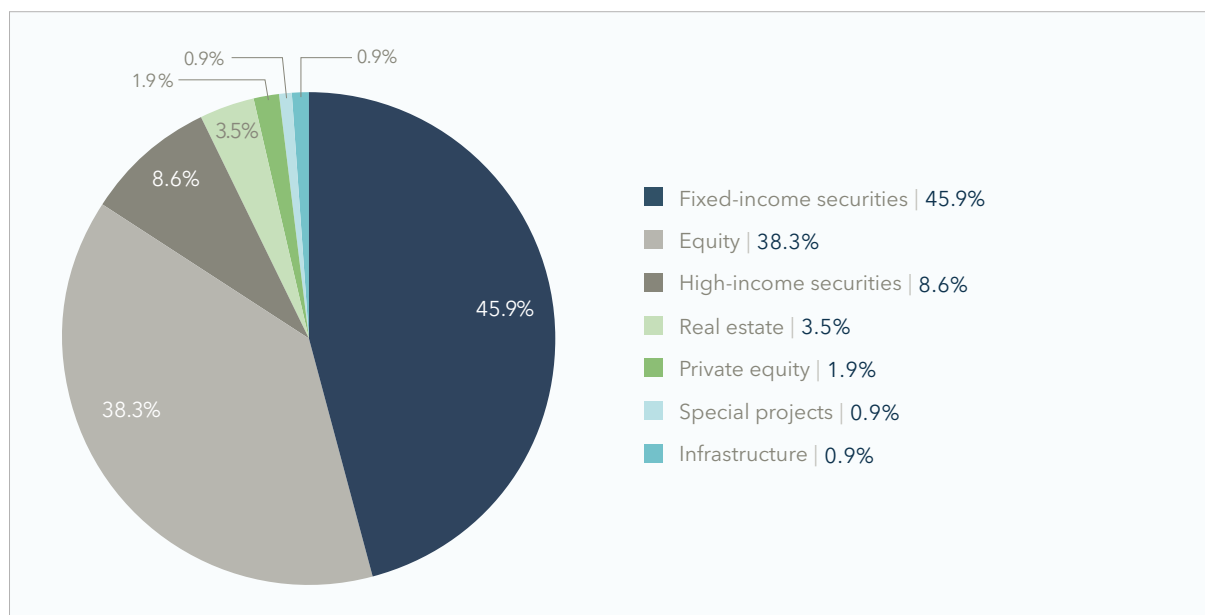




Assets

Standard asset mix 2017

• Figure 3: Standard asset mix 2016



PME investment performance

• Figure 4: Actual returns and benchmark returns

Return	Portfolio	Benchmark	Outperformance
Return inclusive of interest rate hedge	10.3%	10.1%	0.2%
Interest rate hedge*	1.6%	1.6%	0.0%
Return exclusive of interest rate hedge	8.7%	8.5%	0.2%
- Fixed-income securities	6.8%	6.5%	0.3%
- High-income securities	12.3%	12.8%	(0.5%)
- Equity	9.9%	9.5%	0.4%
- Private Equity	11.1%	10.9%	0.2%
- Real estate	8.1%	9.9%	(1.8%)
- Infrastructure	13.1%	13.2%	(0.1%)
- Alternative investments	12.7%	7.0%	5.7%
*Contribution to total return			



Key figures

Numbers at December 31	2016	2015	2014	2013	2012
Employers participating	1,339	1,298	1,282	1,259	1,296
Members (1)	150,136	147,635	147,429	144,407	146,029
- employed by an exempt company (although participating in the TOP scheme)	4,380	5,841	6,188	6,233	7,491
Members in PME basic schem	145,756	141,794	141,241	138,174	138,538
- contributory	138,372	135,595	135,112	132,381	132,818
- non-contributory due to incapacity for work	7,384	6,199	6,129	5,793	5,720
Former members (2)	306,595	302,435	309,449	316,644	320,965
Pensioners (3)	166,419	165,715	167,298	164,563	165,267
Retirement pensions (temporary retirement incl.)	109,355	108,451	110,291	108,390	109,004
Widow's, widower's and partner's pensions	55,479	55,666	55,547	54,769	54,844
Orphan's pensions	1,585	1,598	1,460	1,404	1,419
Total (1+2+3)	623,150	615,785	624,176	625,614	632,261
Members in supplementary schemes					
Pension accrual over and above maximum salary	7,660	7,530	6,774	6,713	7,201
Risk cover for dependant's pension over variable salary	1,250	1,240	1,255	1,351	1,364
Members with disability top-up pension	5,024	4,987	4,988	4,808	4,782
Members with dependant's benefit shortfall pension	8,842	8,878	9,214	10,068	15,231
Cash in (= <i>commutation of pension benefits</i>)	8,469	15,806	13,806	-	-
Active members					
Average salaris (x € 1, rounded up to € 100)	45,200	45,000	44,200	43,200	42,300
Average age (in years)	46.4	46.6	46.3	45.6	45.2



Pension liabilities and pension assets (Amount x € 1 million)	2016	2015	2014	2013	2012
Pension liabilities					
Active members	19,821	17,617	16,231	11,954	12,403
Former members	9,465	8,295	7,041	5,203	5,254
Pensioners	16,992	16,212	15,610	13,847	14,721
Conscientious objectors	3	3	3	3	3
Total pension liabilities (A)	46,281	42,127	38,885	31,007	32,381
Market interest rate liabilities (UFR)	1.36%	1.72%	1.93%	2.77%	2.46%
Other provisions (conditional supplemental pension)	105	79	61	25	85
Premium equalisation account	132	112	n/a	n/a	n/a
Unappropriated reserve (B)	(1,779)	(1,630)	650	1,328	(404)
Assets pertaining to funding ratio (C= A+B)	44,502	40,497	39,535	32,335	31,977
Funding ratio (D = C / A)	96.2%	96.1%	101.7%	104.3%	98.8%
Policy cover ratio ¹	91.8%	97.6%	104.1%	n/a	n/a
Real funding ratio ²	75.2%	79.3%	n/a	n/a	n/a
<p>¹ Under the amended Financial Assessment Framework (FTK) the policy funding ratio became applicable. From 2015 onwards this ratio is used to assess whether a pension fund meets regulatory minimum capital base requirements. The policy funding ratio is calculated as the median of funding ratios reported to the Netherlands central bank DNB at the end of each month over the last 12 months.</p> <p>² The real funding ratio makes clear whether a pension fund can increase future pension benefits in line with the consumer price index. If a pension fund has a funding ratio of 100%, this means it has exactly enough financial means to cover not only its nominal pension liabilities but also conditional indexation (based on full indexation to consumer prices. The stipulated calculation methodology is set out in the Pension Act (133bPW).</p>					



⁴ The pension scheme was amended with effect from 1 January 2006. For participants born before 1950 the previous scheme remains largely valid. In 2016 pension accrual for this group is based on a contribution-free threshold of € 19,643 (2017: € 19,443). The applicable contribution-free threshold for premium payments for all age categories in 2016 was € 15,104 (2017: € 14,904).



Other results	2016	2015	2014	2013	2012
Balanced value transfers (x € 1 million)					
Incoming pension transfers	20	773	1,642	230	2,787
Outgoing pension transfers	1	58	243	35	1
Administration costs (x € 1 million)					
Pension administration costs recurrent	37	36	32	31	30
Pension administration costs non-recurrent/ investment	5	3	4	6	4
Direct investment costs	77	61	58	57	55
Totals costs in financial statements	119	100	94	94	89
Overall asset management costs including direct investment costs	168	161	144	129	161
Assets (x € 1 million)					
<i>Portfolio construction at year-end⁵</i>					
Real estate	1,500	2,020	2,127	2,126	2,253
Equity	17,896	14,960	13,852	9,937	8,084
Fixed-income securities	24,588	22,112	22,647	19,297	20,165
Other investments	615	1,376	719	909	1,368
Total assets invested	44,599	40,468	39,345	32,269	31,870
<i>Portfolio construction at year-end⁵</i>					
Real estate	3.4%	5.0%	5.4%	6.6%	7.1%
Equity	40.1%	37.0%	35.2%	30.8%	25.3%
Fixed-income securities	55.1%	54.6%	57.6%	59.8%	63.3%
Other investments	1.4%	3.4%	1.8%	2.8%	4.3%
Total assets invested	100.0%	100.0%	100.0%	100.0%	100.0%
<i>Total returns by invested categorie⁵</i>					
Real estate	144	220	246	(28)	33
Equity	1,616	1,105	1,788	1,230	946
Fixed-income securities	1,716	212	2,931	(740)	1,663
Other investments	642	(1,106)	965	(162)	1,037
Total returns on assets invested	4,118	431	5,930	300	3,679
<i>Total returns by invested categorie⁵</i>					
Real estate	9.1%	12.1%	9.0%	1.3%	2.0%
Equity	10.0%	4.2%	11.5%	18.7%	15.6%
Fixed-income securities	9.9%	(1.9%)	22.6%	(6.2%)	14.8%
Other investments'	15.7%	(4.4%)	8.0%	(4.8%)	(1.9%)

⁵ In the key figures the investment categories (mix and returns) are presented in accordance with the strategic investment policy as of January 2015.



Assets - continued	2016	2015	2014	2013	2012
<i>Return on total assets invested</i>					
Total return	10.3%	1.0%	17.8%	1.0%	13.0%
- of which direct return	3.1%	3.2%	2.1%	2.2%	2.1%
<i>Z-score</i>					
Z-score per annum	0.38	0.44	0.25	0.21	0.07
Performance test ⁶	1.89	1.73	2.22	1.22	(0.28)
Euro/U.S. dollar exchange rate	1.05	1.09	1.21	1.30	1.32

⁶ The performance test shows to what extent the actual investment returns achieved over a period of five years deviate from the investment returns on the benchmark portfolio over that same period. For performance test review purposes, the outcome of this test (as described in Schedule 1 to the Dutch Industry Pension Funds (Exemption and Penalties) Decree 2000) is presented plus 1.28. The performance test is passed if the outcome is equal to or greater than nil.

The average company in the Metal and Electrical Engineering Industry

In 2016, the average affiliated company had 109 employees who were accruing pension and of which 103 were active and 6 fully or partially incapacitated for work. Of the 109 employees, 14 were female and 95 male. The average age of the employees was 45 years for women and 47 years for men. In 2016, the average company had 82 former employees who received an old-age pension or TOP (an early retirement scheme operated by PME) payment and 43 surviving dependants of former employees with a surviving dependants' pension.

In 2016 the average company and its employees together paid € 705.751 in premiums towards the old-age pension. At the end of 2016, the average pension assets for each member company was € 33,2 million. In 2016, € 6.483 was paid in premiums for the basic scheme for the average employee. Of that sum, the employee paid a maximum of half, or € 3.242.



About PME

PME is the pension fund of the Metal and Electrical Engineering Industry (Metalektro). PME works on behalf of more than 1300 companies and more than 145,000 participants. In addition, around 166,000 pensioners receive a monthly payment. PME also manages the pension entitlements of more than 306,000 former participants. PME is the fund for companies in the metal and electrical engineering industry which in general have more than 30 employees. This means that we work for both small and very large companies. We provide pensions for those people in the Netherlands who know how technology works. They make things in metal and electrical engineering, develop new inventions and assist in assembly and installation. It is a broad and highly-developed sector. Ships are designed and built. Microchip machines are developed and microchips made. Car and lorries. Steel in every conceivable form. From miniscule hi-tech to heavy industry. The sector operates on a national and international level and the leading companies attract highly specialised employees from the Netherlands and the rest of the world.

Our mission

PME's mission is to administer the pension scheme of the Metal and Electrical Engineering Industry in a proper, balanced and cost-effective manner. In doing so, PME aims to achieve as good a pension as possible at the lowest possible cost. PME invests and manages the pension premiums at sensible risk levels and in a socially responsible manner.

In fulfilling this mission, PME's strategy is as follows:

- to achieve correct pension administration and asset management;
- to obtain as high a yield as possible within the established risk and administration frameworks. Important aspects in this regard include sustainability, cost reductions and the reduction of complexity;
- to optimise the service provided to employers and participants in the sector and to increase their pension awareness;
- Restoration of confidence in the pension fund, among things through greater clarity towards and visibility in the media. This means a more proactive attitude, making clear that PME defends the interests of its participants.
- Enhancement of simplicity in participant and employer administration and attainment of advantages of scale through procedural harmonisation. This will be sought through close cooperation with other pension funds, specifically *Pensioenfondsen Metaal en Techniek* (PMT).

Management

Since 1st July 2014, PME has had a one-tier board. We believe this management model allows us to best fulfil the necessary requirements in the area of expertise, suitability and availability. PME has 2 fund bodies: the management board and the accountability committee.

The management board consists of 1 independent chairperson, 3 independent executive directors and 8 supervisory non-executive directors.

The non-executive directors are representatives of the various groups of stakeholders: employees, employers and pensioners. The 3 executive directors are together responsible for the day-to-day management of the fund. They are full-time employees of the fund. Of the 8 non-executive directors, 4 represent the employers' organisations, 2 represent the employees' organisations and 2 represent the pensioners. The 8 non-executive directors supervise the 3 executive directors and together with the executive directors and the independent chairperson they are responsible for the general policy and strategy of the fund.



PME executive day-to-day management

The following executive directors are responsible for the day-to-day management of PME:

Eric Uijen (1959), General Director of PME

Management role: Executive Director - Strategy & Policy, Finance, Control & Risk Management

Marcel Andringa (1970)

Management role: Executive Director - Asset Management

Vacant year end 2016

Management role: Executive Director - Pension Management & Communication

Non-executive board

The General Board of PME consists of eight non-executive directors: four on behalf of the employers, two on behalf of the employees and two on behalf of the pensioners.

Chairman of the board

Franswillem Briët is the independent chairman of the board.

Accountability body

The management of the pension fund is accountable to the accountability body with regard to its policy and the implementation thereof. The accountability body may express an opinion regarding the actions and policy of the management and policy decisions for the future. The accountability body also has the right to issue advice. This right to issue advice concerns, amongst other things, the fund's remuneration policy, the form and organisation of internal supervision, communication policy, the joining of new pension funds and the administration agreement.



Colophon

Design

Myriad Design, Amsterdam

Text

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www.metalektropensioen.nl