

May 2021 GAD information notes

Each month we update the interest index within the model. The Index is based on the guaranteed rate of interest from the 5-year Fixed Interest Savings Certificates (FISC) from National Savings & Investments. This savings product is no longer on general sale, except for customers with maturing 5-year Fixed Interest Savings Certificates (FISC). We have updated this month's model with the latest rate of interest applicable. (see link <https://www.nsandi.com/historical-interest-rates#09>)

The annual interest rate for the 5-year FISC had changed with effect from 1 May 2020, reducing from 1.9% to 1.6%. However, the "historical interest rates" webpage (link in bullet 1 above), which GAD use as the source of the interest rates was not updated until November 2020. As a result the models issued between June 2020 to November 2020 contain the incorrect interest index numbers. The error will impact quotations with a calculation date after 1 May 2020.

Future updates

In order to avoid this issue occurring again, before issuing future models GAD will cross reference the "historical interest rates" section of the NS&I website with more recent NS&I announcements, and other external websites, as an additional check.

Materiality impact of correcting interest index

An annual interest rate of 1.6% can be expressed as a *monthly interest rate of 0.1333%*. Similarly, an annual interest rate of 1.9% can be expressed as a *monthly interest rate of 0.1533%*. [Note $0.1533\% - 0.1333\% = 0.025\%$, which is the difference in the monthly interest rate.]

So therefore, calculations after one month (at end May 2020) in a corrected model would provide a cost quote that is 0.025% smaller. For calculations after two months (at end June 2020) a corrected model would provide a cost quote that is 0.05% smaller [two months' worth of the 0.025% monthly interest rate] and so on. For calculations after six months or more (at end October 2020 or later) a corrected model would provide a cost quote that is 0.15% smaller. (For example, if the quoted cost was £1,001.50 the corrected cost might be £1,000.)

All else being equal, a correction to the model/index would mean cost quotations may be **up to 0.15% smaller**. A model correction of 0.15% would generally fall below any materiality threshold. Therefore, we do not propose updating and re-issuing those models.

Changes to the average earnings index

The settlement model uses an index relating to earnings known as the Average Earning Index (AEI) (LMNQ series). This index tracks movements in earnings for the UK whole economy, including bonuses and is seasonally adjusted. The Office for National Statistics has announced that the AEI has been discontinued as it is no longer the lead measure of short term changes in earnings and has been replaced by the Average Weekly Earnings (AWE) statistic (see <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandwork/inghours/datasets/averageweeklyearningsearn01> and <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandwork/inghours/timeseries/kab9/>).

The broadly equivalent AWE statistic is the KAB9 series, which follows changes in earnings for the whole economy, including bonuses, and is seasonally adjusted. The KAB9 statistic will be used in this month's, and future months', settlement models.

If you are content with the use of the AWE (KAB9 series) statistic then you do not need to respond to this email. However, please contact us if you need further information or would like us to consider the use of an alternative index so that we can consult with HM Treasury.

Please note that the earnings index underlying the monthly Preston settlement models (and associated models) issued with effect from July 2017 have been amended to allow for the rebased EARN01: KAB9 series statistic (see announcement for more information:

<https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinhours/articles/improvementstoearningsestimatesforsmallbusinessesinaverageweeklyearnings/2017>).

You may wish to check and amend your scheme's Preston documentation so that any references to AEI should now state the AEI has been discontinued and the AWE will be used instead. GAD has alerted HM Treasury that their Preston guidance on their website will need to refer to AWE.