October 2020

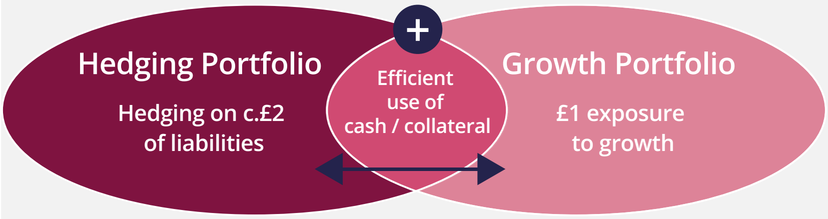
Liability hedging without sacrificing return potential

This communication is for investment professionals only and should not be distributed to or relied upon by retail clients. It is only intended for use in jurisdictions where the relevant funds are authorised for distribution or where no such authorisation is required.

Liability Aware Equity

Many DB pension schemes currently have an allocation to equities within their asset portfolio to provide growth exposure with the aim of outperforming the liabilities and improving the funding level over time. Traditionally an allocation to growth assets, such as equities, reduces the available allocation to bond / hedging assets. This therefore limits the ability for schemes to meet two important objectives – improving the funding position over time through asset growth and achieving a high level of interest rate and inflation hedging to protect the scheme's funding level against liability risks.

With our Liability Aware Equity (LA Equity) funds, schemes can now maintain exposure to equities, whilst increasing their level of liability hedging. The LA Equity funds are an extension to our Integrated Liability Plus Solutions (ILPS) fund range, with the growth engine targeting returns in line with passive unhedged global equity markets (MSCI All Country World Index).

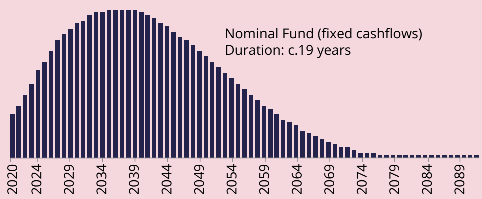
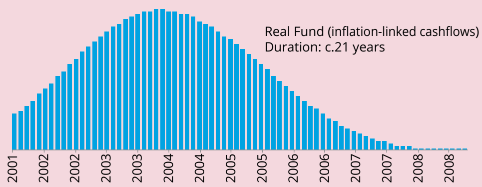


Every £1 invested in an ILPS fund has two obectives:

- **Hedging Portfolio** – To provide c.£2 hedging against changes in the value of liabilities arising from movements in interest rates and (in the Real Funds) inflation expectations.
- **Growth Portfolio** – At the same time, to seek a return in excess of cash on the £1 invested in the fund.

What do the LA Equity funds provide?

- **An efficient solution to increase hedging** – Every £1 invested in the LA Equity funds provides c.£2 protection on the liabilities, making them an efficient solution to manage liability risk.
- **Ability to retain equity exposure** – Many pension schemes already have an allocation to equities. In this case, they may wish to retain their equity exposure but at the same time also increase their hedging.
- **Low governance solution** – The LA Equity funds offers a simple, low governance solution to pension schemes, with easy implementation and ongoing support.

	Liability Aware Absolute Return II (LA AR II)	Liability Aware Absolute Return III (LA AR III)	Liability Aware Equity (LA Equity)
Heding Portfolio			
Profiles	ILPS funds make use of two simple liability cashflow profiles based on the average pension scheme.  		
Target hedging multiple	The ILPS funds target an indicatie liability hedging multiple of 2x		
Growth Engine			
Return Target*	3 Month LIBOR	6 month LIBOR +5% pa	In line with global equity markets
Expected Volatility**	2% to 4%	4% to 8%	In line with global equity markets
Ideas Universe	Bonds and FX Macro	Multi-Asset Macro	Global Equity (MSCI ACWI)

Source: Aberdeen Standard Investments.
* Return targets are annualised return, gross of fees, evaluated over rolling 3 year periods.
** Risk measure is annualised volatility.

Aberdeen Standard Investments

Hedging portfolio

As with all ILPS funds, the Hedging Portfolios cover circa £2 of liability value for each £1 invested, providing capital efficiency. Clients can choose either **nominal (fixed) or real (inflation-linked) interest rate hedging**, based on two average pension scheme liability cashflow profiles.

Growth portfolio

In addition to hedging interest rate and inflation risk, every £1 invested in the fund also targets returns **in line with (unhedged) global equities.**

This is achieved through synthetic exposure to the MSCI All Country World Index (ACWI), meaning investors receive **a total return on global equities.**

The fund seeks to replicate physically investing in unhedged global equities. Therefore, the equity **return will have two components – local equity market performance and currency returns vs GBP.**

Case study

The scheme

- A DB pension scheme with a funding deficit and low level of hedging. The scheme has an existing LDI mandate in place alongside corporate bonds, equities and absolute return/ diversified growth funds.

Key objectives

- The client is looking to (1) increase level of liability hedging to around 80%; and (2) not sacrifice growth asset exposure required to support funding basis.

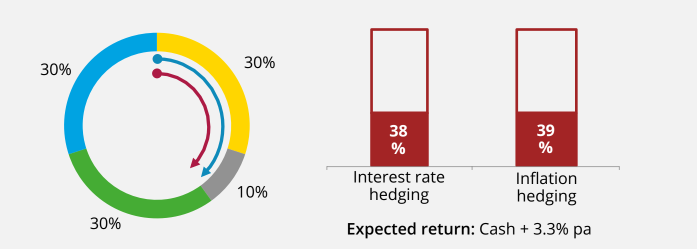
Potential solution

- The client allocates a proportion of their equity holding into the Liability Aware Equity funds.

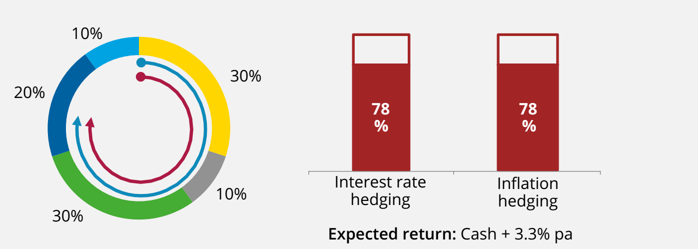
Key outcomes

- No material change to growth asset allocation exposure – in particular no decrease in equity exposure or impact on growth return potential.
- Level of interest rate and inflation hedging significantly increased.

Before Changes



After Changes



- Corporate Bonds
- External LDI profile fund
- External DGF
- LA Equity
- Equities
- Interest Rate Hedging
- Equities

Important Information

The value of an investment is not guaranteed and may go down as well as up. Past performance is not a guide to future performance. This document is for information only and does not constitute investment advice. We recommend you seek professional advice before deciding whether to invest in this product. Please refer to the relevant offering documents for more details of the risks applicable to each fund.

Standard Life Investments Limited is registered in Scotland (SC123321) at 1 George Street, Edinburgh EH2 2LL. It is authorised and regulated in the UK by the Financial Conduct Authority and is the Investment Adviser and Distributor for Standard Life Investments Liability Solutions ICAV. Aberdeen Standard Investments Luxembourg S.A is a company incorporated under the laws of the Grand Duchy of Luxembourg and having its registered office at 35a, avenue John F. Kennedy, L-1855 Luxembourg, Grand Duchy of Luxembourg. It is authorised in Luxembourg and regulated by the CSSF and is the Authorised Investment Fund Manager for Standard Life Investments Liability Solutions ICAV.

Standard Life Investments Liability Solutions ICAV is regulated by the Central Bank of Ireland and is an openended umbrella fund with segregated liability between sub-funds registered in the Republic of Ireland (no. C142122) at 70 Sir John Rogerson's Quay, Dublin 2, Ireland.