February 2019

A tailored approach to Cashflow Driven Investment

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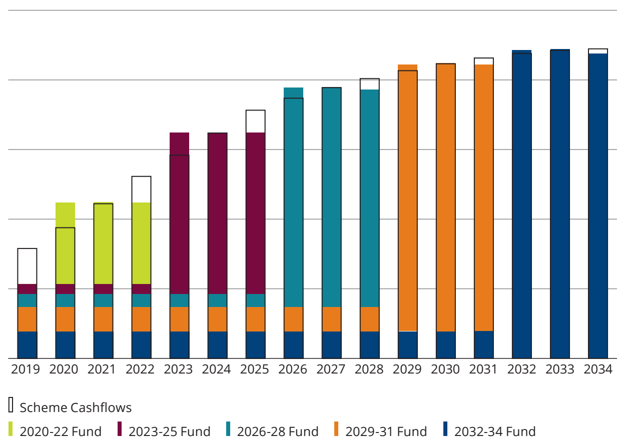
Liability Aware CDI Funds

Following closure to new members, many DB pension schemes are now becoming **cashflow negative**, i.e. where benefit outgo exceeds income from contributions and investments. Many schemes are therefore paying more attention to arranging their assets to deliver the income required to pay benefits, often referred to as "**Cashflow Driven Investment**" or "CDI".

For larger pension schemes targeting self-sufficiency, a segregated approach may be appropriate; however, for small to medium sized pension schemes a pooled solution may be more suitable. Our **Liability Aware CDI fund range** can be used by pension schemes to create a bespoke cashflow payment profile that fits their particular scheme's future cashflow requirements after allowing for contributions and income from other assets such as private debt or real estate.

What are the Liability Aware CDI funds?

- The Liability Aware CDI fund range consists of five 3-year "buckets", **allowing pension schemes to tailor their holdings to meet their cashflow requirements.** New funds will be created as existing funds mature. It is also our intention to launch longer-dated credit and gilt options in the near future.
- They are a series of maturity dated cashflow funds, managed on a buy & maintain basis that look to deliver a **relatively predictable series of cashflow** from a portfolio of nominal corporate bonds – with coupons and redemption proceeds paid out over time.
- The funds are expected to invest in nominal **GBP corporate bonds** only at outset (**targeting an average credit quality of A**). The funds are also permitted to hold gilts and derivatives (including CDS) and overseas bonds if these become appropriate to manage the portfolio efficiently.



Why invest in Liability Aware CDI?

Compared to a simple buy & maintain credit fund where cashflows may vary over time, a CDI approach has an explicit goal of maintaining the shape of the cashflow profile.

- **Precision and certainty of cashflow delivery** – rather than maximise return, the objective of each fund is to maintain a relatively stable pay-out profile per unit held.
- **Ability to create a bespoke solution for your scheme** – by combining allocations across the fund range.
- **Strong track record of avoiding defaults and downgrades** – managed by our Credit team consisting of over 140 portfolio managers and analysts based across Europe, North America, Asia and Australia.

Why ASI for Cashflow Driven Investment?

- ✔ **Our heritage** – ability to leverage our insurance heritage and deliver credible CDI solutions
- ✔ **Our experience** – we manage over £32.5 billion across 38 Buy & Maintain Credit mandates
- ✔ **Our highly regarded credit team** – with a strong track record of avoiding downgrades and defaults
- ✔ **Our wider asset capabilities** – including access to illiquid credit and other assets offering alternative sources of income
- ✔ **Our approach to working in partnership with our clients and their advisers** – to ensure we meet their evolving needs.

Aberdeen Standard Investments

Case Study

A mature and cashflow negative DB pension scheme with c.£150m of assets, underfunded on a low risk basis looking to review the investment strategy.

Although the scheme had invested a proportion of assets in bonds (credit and LDI), the pooled funds used provided minimal income and so the scheme was having to regularly disinvest over time to meet benefit payments.

Key objectives

The key objectives from a new investment strategy were to:

1. Achieve sufficient return above gilts to close the funding gap over time; and
2. Limit disinvestment risk by investing a proportion of assets to provide income to meet expected future cashflow over the short to medium term

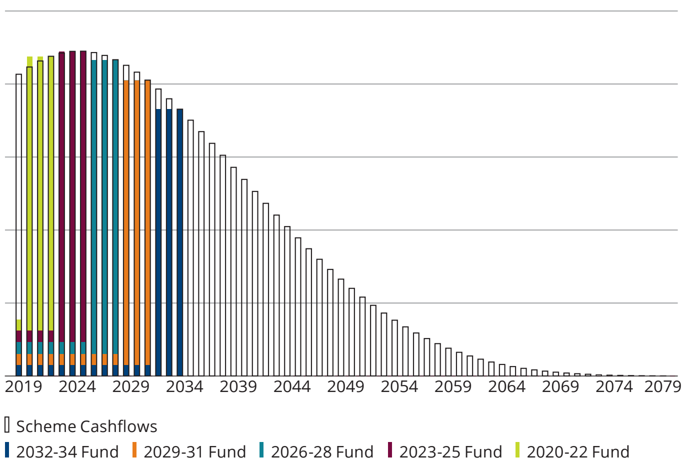
Solution to meet the client's objectives

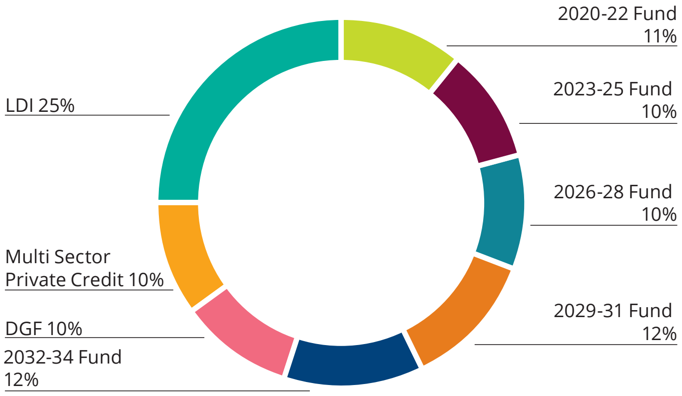
Working with the scheme's consultant, a solution was developed using a combination of the five CDI funds to match the first 15 years of expected liability cashflows as shown in the chart opposite. The analysis suggested that around 55% of the scheme's assets would be required to be invested in the CDI funds.

The remaining assets (c45%), were invested in a range of long-term strategies including multi sector private credit and diversified growth funds, as well as LDI to hedge a proportion of interest rate and inflation risk.

By matching the first 15 years of cashflow using Liability Aware CDI funds, the client became a genuine long-term investor for the remaining assets with limited risk of having to disinvest growth assets at short notice.

Over time, the scheme expects to switch from growth assets into longer-dated CDI funds as the funding position improves.





Key outcomes

Limited disinvestment / reinvestment risk over the next 15 years as asset income provided to meet future cashflow requirements.	Higher certainty of return from CDI solution versus typical buy and maintain corporate bond funds.	Genuine long-term investor for growth asset strategies. Low risk of becoming a forced seller of assets.

Important Information

For professional investors only – Not for use by retail investors.

Investors should be aware that past performance is not a guide to future results. The value of investments, and the income from them, can go down and your clients may get back less than the amount invested.

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121035865 02/19 | DH: GB-120219-82683-1