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Press Release

For immediate release
2 November 2009

Q3 sees record levels of inflation hedging by UK pension schemes

UK pension funds hedged over £11.4bn liabilities during the third quarter of the year, according to estimates included in the latest F&C Liability Driven Investments (LDI) Survey, released today. This figure registers as the largest amount of inflation hedging recorded over the last seven quarters since the survey started.

The F&C LDI Survey is conducted on a quarterly basis by F&C's Asset Liability Management (ALM) team and based on responses from the derivatives trading desks most closely involved in pension liability hedging at major investment banks.

The survey's results suggest that schemes that missed earlier opportunities in the first half of the year to hedge at attractive inflation levels, rushed into the market during the third quarter. This, combined with notably better inflation supply, meant the quarter was characterised by much better liquidity and lower transaction costs.

Alex Soulsby, Derivatives Fund Manager at F&C's LDI team, said: "Our latest survey points out that, although better opportunities were available earlier in the year, prices in Q3 were still much better than last year and so pension schemes have continued to hedge RPI on fears that inflation is only heading in one direction - up. "

The results show that there was less nominal hedging than inflation hedging for the first time since the launch of the survey, with interest rate hedging levels even lower than during the chaotic last quarter of 2008. (see tables).

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The survey also asks investment banks derivatives desks for their opinions on the likely direction of key rates for pensions liability hedging. For the forth quarter of 2009, there is the strongest consensus in the direction of yields since the start of the survey, with the majority of respondents expecting rises in nominal, inflation ad real years.

Soulsby added: “The findings very much mirror the sentiment of trustees whose primary concern is a fear of rising inflation, while they expect UK interest rates to rise. Those who support this view cite the burden of government borrowing, inflation, economic recovery and the end of quantitative easing. Because many pension schemes set target levels at which their fund managers should act, the downward move in rates over the quarter may have postponed potential hedging. “

Table 1: Risk – Volume of UK Pension Liability Hedging in (£ per 0.01% change in interest rates or RPI inflation)

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09
Interest Rates	24,545,000	22,925,000	22,725,000	19,200,000	20,100,000	23,775,000	17,465,000
Inflation	13,735,000	12,590,000	13,325,000	14,650,000	15,000,000	22,600,000	22,885,000

Table 2: Liabilities Hedged (F&C Estimate)

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09
Interest Rates	9,327,000,000	8,712,000,000	8,635,500,000	7,296,000,000	7,638,000,000	9,034,500,000	6,636,700,000
Inflation	6,868,000,000	6,295,000,000	6,662,500,000	7,325,000,000	7,500,000,000	11,300,000,000	11,442,500,000

- Ends -

To obtain a copy of the survey or further information on F&C’s LDI solutions please contact F&C’s communications team on +44 (0)20 7011 4600

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Notes to Editors

Liability Driven Investment at F&C

- F&C is among the leaders in offering flexible and robust LDI solutions designed to mimic a pension funds’ sensitivity to interest rates and inflation.

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- F&C's LDI pooled solution invests in interest rate and inflation derivatives to hedge the pension scheme's liability sensitivities and also in assets that are expected to give a return of 3 month GBP LIBOR over a 3 year investment horizon.
- These pools have on average a leverage of 3 times, meaning a typical fully-funded pension fund can hedge 100% of its liability by only investing 33% of its assets into F&C's LDI pools, thereby allowing the scheme to allocate the majority of its assets into return generating investments.

F&C Investments

- F&C Asset Management (F&C) is an independent London Stock Exchange listed asset management group with around 100,000 shareholders.
- F&C traces its origins to 1868 with the launch of the Foreign & Colonial Investment Trust, the first ever publicly listed investment fund. Foreign & Colonial Investment Trust remains a client of F&C.
- F&C is an active fund manager with a multi-specialist investment model where individual teams have strong accountability for their products and processes. The group is also an active shareholder with a leading franchise in governance and sustainable investment.
- F&C manages £99.2 billion (€108.5 billion) of assets** for a diverse range of institutional, insurance and retail clients across all major asset classes – equities, bonds, cash and property – as well as alternative and specialist product classes such as Socially Responsible Investment funds, hedge funds, private equity funds and Liability Driven Investments. F&C invests globally and has been a longstanding investor in emerging markets.
- F&C REIT Asset Management is the group's global property asset management business. It was formed in 2008 from the merger of F&C's property division and REIT Asset Management. F&C REIT operates from offices in London, Dublin, Munich, Mumbai and Stockholm.
- F&C manages assets principally from three investment centres: London, Amsterdam and Edinburgh. The group has a global office network spanning a dozen countries: China (Hong Kong), France (Paris), Germany (Frankfurt & Munich), India (Mumbai), Ireland (Dublin), The Netherlands (Amsterdam), Portugal (Lisbon), Sweden (Stockholm), Switzerland (Geneva), UK (London, Edinburgh, Dorking) and the United States (Boston).
- In March 2009 F&C signed a Memorandum of Agreement with Hua Xia Bank, one of China's twelve nationwide joint stock commercial banks, to establish a joint venture fund management company in China in which F&C will have a 19.5% interest.

** As at 30 September 2009.

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