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Press Release

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Inflation hedging takes a back seat as pension schemes play the waiting game

Inflation hedging by UK pension schemes showed a significant decrease in the last quarter of 2009, according to estimates included in the latest F&C Liability Driven Investments (LDI) Survey.

The F&C LDI Survey is conducted on a quarterly basis by F&C's Asset Liability Management (ALM) team and is based on responses from the derivatives trading desks most closely involved in pension liability hedging at major investment banks. The Q4 results show a 37% fall in inflation hedging compared with the previous quarter (see tables).

The survey points at market levels being less attractive during Q4 – with lows set right at the start of the quarter – as one of the reasons for this fall. Levels rose following the linker syndication at the end of September and schemes which missed that opportunity may have decided to wait for the next linker syndication at the end of January to implement inflation hedging strategies. In addition inflation fears remain a concern among trustees, and F&C expects any fall in inflation rates to stoke demand.

Nominal hedging remained low, only slightly above the previous quarter's number which was the lowest figure since the survey was launched two years ago.

Alex Soulsby, derivatives fund manager at F&C, commented: "These figures validate the view that trustees are taking more tactical views and they continue to expect nominal yields to rise in the future. UK government debt is rising sharply and while quantitative easing has more than absorbed the increase in gilt supply, the winding down of that monetary stimulus may lead to a rise in government yields."

Furthermore there has been a marked increase in sovereign risk, reflected by the rise in the CDS rates of countries like the UK, Spain and Ireland.

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F&C Asset Management plc is the listed holding company of the F&C Group.

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Soulsby added: “If the fiscal deficits arising from the crisis are not addressed and the market sees no credible way of the UK restoring balance to its budget and repaying its debts, fears of a rise in government yields will continue. This, coupled with the political uncertainty of an election year and the possibility of a hung government, means we expect more volatility in 2010.”

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

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	Q4 09
Interest Rates	24,545,000	22,925,000	22,725,000	19,200,000	20,100,000	23,775,000	17,465,000	17,545,000
Inflation	13,735,000	12,590,000	13,325,000	14,650,000	15,000,000	22,600,000	22,885,000	14,315,000

Table 2: Liabilities Hedged £ (F&C Estimate)

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	Q4 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	6,666,900,000
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	7,157,500,000

- 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

F&C Investments

- F&C Asset Management (F&C) is an independent London Stock Exchange listed asset management group with around 100,000 shareholders.

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- F&C traces its origins to 1868 with the launch of 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 £97.8 billion (€110.2 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. F&C invests globally and has been a longstanding investor in emerging markets.
- F&C has three pillars to its strategy: *Advisory & Solutions* – the servicing of strategic partners and the provision of investment solutions and overlays such as shareholder engagement programmes, Liability Driven Investments, Asset & Liability Management, Multi-Manager and Fiduciary Management; *Alpha Investing* – active fund management across a diverse range of asset classes and markets but with a focus on UK and European equities and fixed income and Emerging Markets; *Environmental, Social & Governance Investing* – building on its market leading presence in ethical investment with new products.
- 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 31 December 09.