Capita

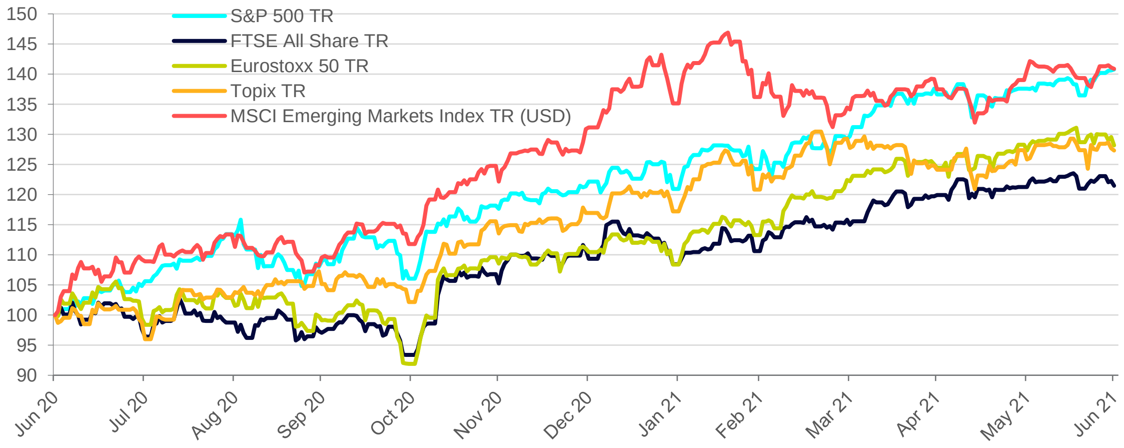
Quarterly Investment Bulletin

June 2021

Contents

Global equities continued to rise over the quarter

Figure 1: Equity market returns (rebased at 100) [1]



Source: Bloomberg, Capita

Equity Markets	Percentage Change			
Index	**30/06/2021 (Price)**	**1 Month**	**1 Quarter**	**1 Year**
S&P 500 (TR)	8943	2.3%	8.5%	40.8%
FTSE ALL-Share (TR)	7852	0.2%	5.6%	21.5%
EuroStoxx 50 (TR)	8931	0.7%	4.9%	28.2%
Topix (TR)	3071	1.2%	-0.3%	27.3%
MSCI Emerging Markets Index TR (USD)	671	0.2%	5.0%	40.9%

Source: Bloomberg, Capita | [1] Total returns in local currency

- Global equities generally continued to see improvements over the second quarter of 2021, with markets now comfortably ahead of pre-Covid-19 levels. All major indices made positive returns over the quarter, apart from Topix which returned -0.3%.
- US equities posted a strong quarter of positive performance, rising by +8.5%. This means that the S&P 500 index is now up by +40.8% since the end of June 2020.
- The FTSE All-Share index continued to see improved growth with returns of +5.6% over the quarter. The UK Equity market is now up by 21.5% since end June 2020.
- In the eurozone, the EuroStoxx 50 index returned +4.9% over the quarter. European equities are now up by 28.2% since end June 2020.
- In Japan, the Topix index fell slightly over the quarter, returning around -0.3%. However, the Japanese equity market is up +27.3% since the end June 2020, similar to European equities.
- In emerging markets, the MSCI Emerging Markets Index returned +5.0% over the quarter. Emerging Market Equities are now up +40.9% since the end of June 2020, similar to US Equities.

Nominal gilt yields fall slightly across the curve during the quarter

Figure 2: Nominal term structure of gilts

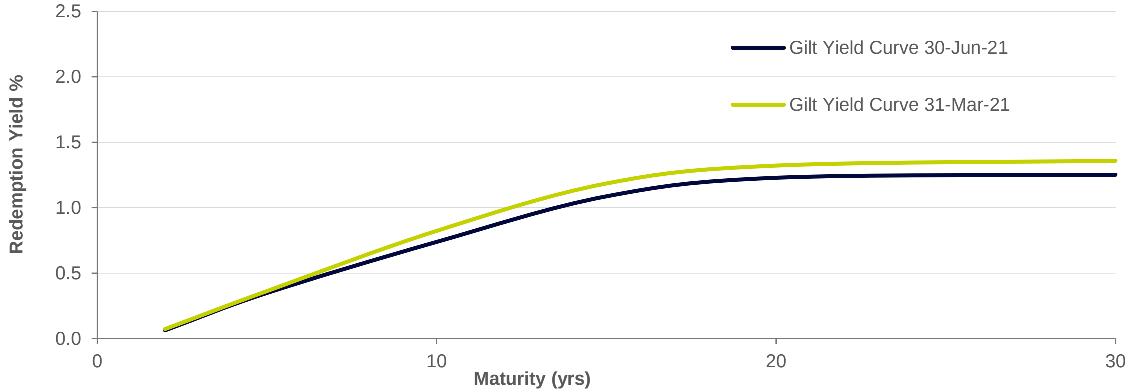
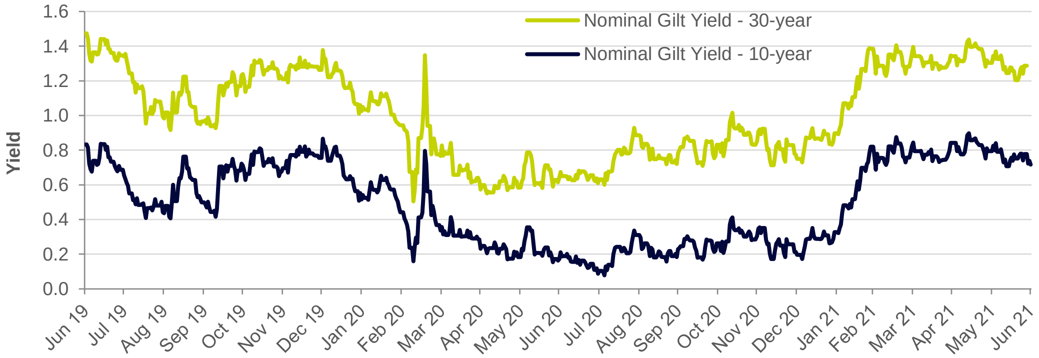
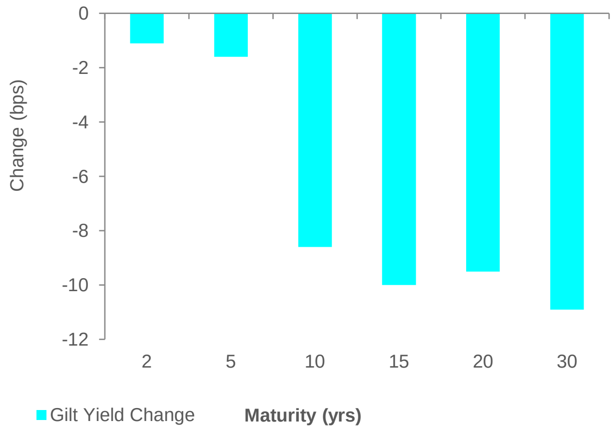


Figure 3: 10-year and 30-year nominal yields



Source: Bloomberg, Capita



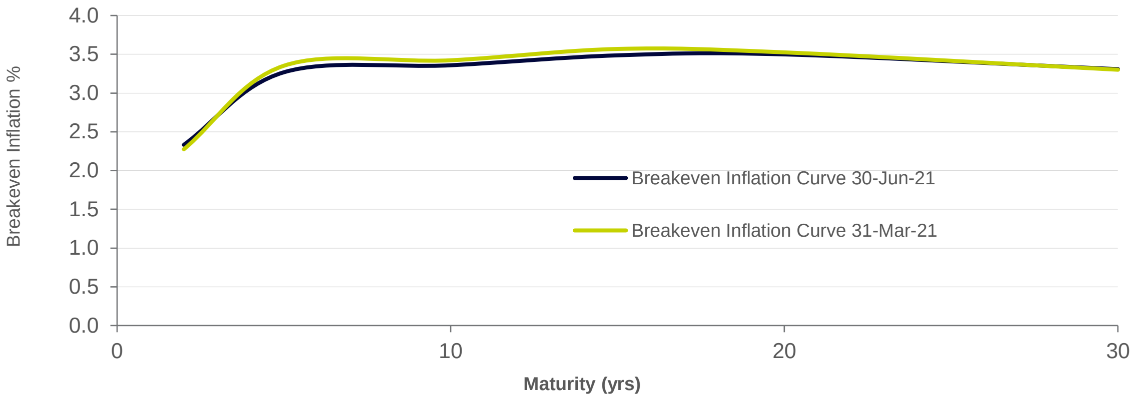
Source: Bloomberg, Capita

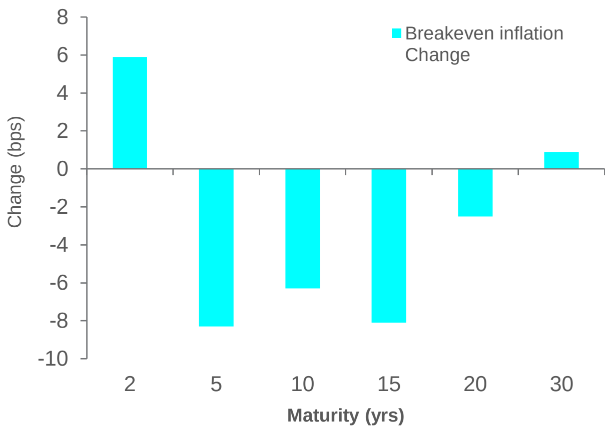
Rise in both gilts yields and growth assets over the year presents opportunities

- Nominal gilt yields decreased slightly across all maturities, over the second quarter of the year.
- The funding level improvements that were seen over the first quarter of 2021 have maintained at a similar level due to the continued rally in growth assets.
- As a reminder, this has presented an attractive de-risking opportunity for some schemes as they have found themselves ahead of where they expected to be on their Journey Plan.
- This is especially true for schemes with relatively low levels of liability hedging (LDI).
- Trigger-based dynamic de-risking strategies, where funding levels are tracked daily and pre-agreed de-risking is undertaken when triggers are hit, are often the most efficient way to capture temporary de-risking opportunities.

Future inflation expectations broadly unchanged
Realised (past) inflation rises over the quarter

Figure 4: Gilt-Implied Future Inflation Expectations [2]

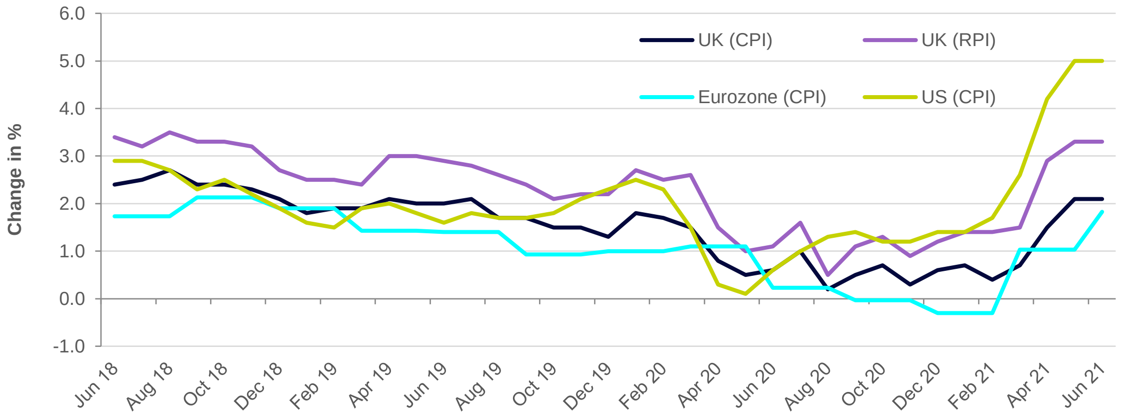




Source: Bloomberg, Capita

[2] Gilt breakeven inflation has been calculated as the difference between nominal Gilt yields and real Gilt yields.

Figure 5: Realised (past) CPI in the UK, US and Eurozone



Source: Bloomberg, Capita

Inflation

- Future inflation expectations maintained at around the same level as the end of June 2021 causing little effect to each maturity, with the biggest effects for the middle turns. This has acted to keep pension scheme liabilities at around the same levels.
- Realised (past) UK CPI inflation rose over the quarter from 1.0% as at end of March (as restated) to 2.1% at end of the quarter [3]. Realised UK RPI, however, was up to 3.3% compared to 1.5% for the end of the previous quarter (as restated).

[3] At the publication date of this bulletin, the ONS had not yet announced the end June CPI and RPI rates so we have used end May figures as the latest available.

Real yields decrease across most of the curve

Figure 6: Gilt real yield[4] term structure

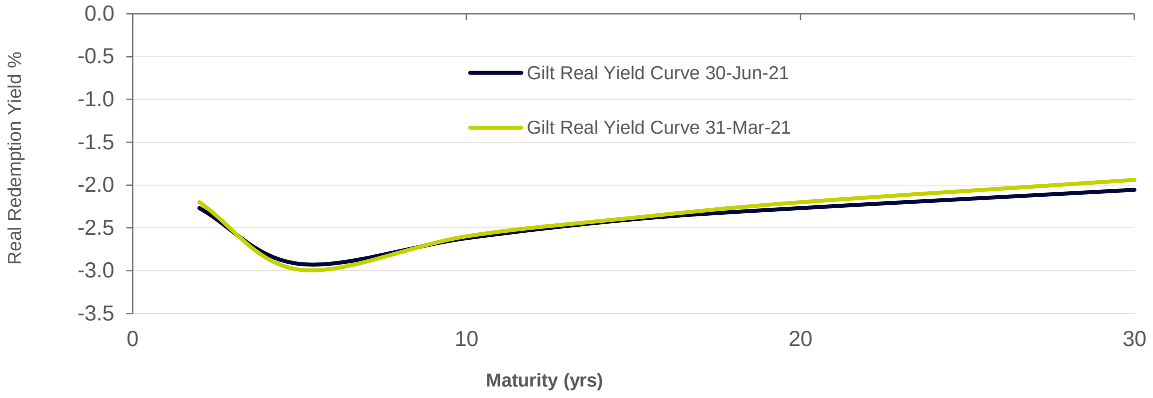
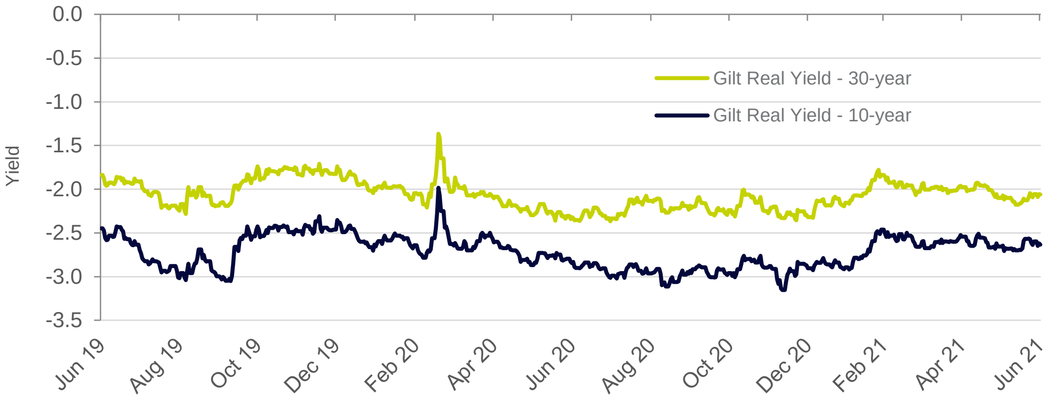
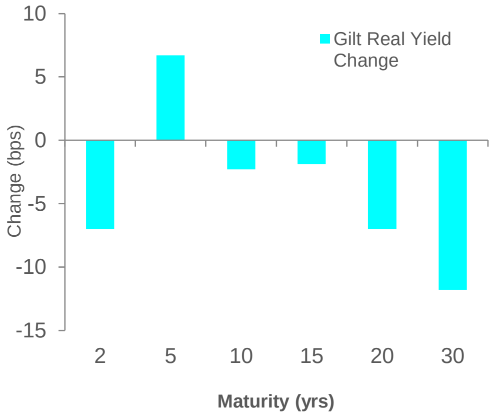


Figure 7: 10-year and 30-year real yields

Source: Bloomberg, Capita





Source: Bloomberg, Capita

Real Gilt Yields	Maturity Points (yrs)					
	2	5	10	15	20	30
Current % as at 30/06/2021	**-2.27**	**-2.92**	**-2.62**	**-2.40**	**-2.27**	**-2.06**
1 Month Change (bps)	4	20	4	-1	4	4
1 Quarter Change (bps)	-7	7	-2	-2	-7	-12
1 Year Change (bps)	25	-18	21	31	25	28

Source: Bloomberg, Capita

[4] Gilt real yield has been calculated as the yield on index-linked Gilts

Real yields

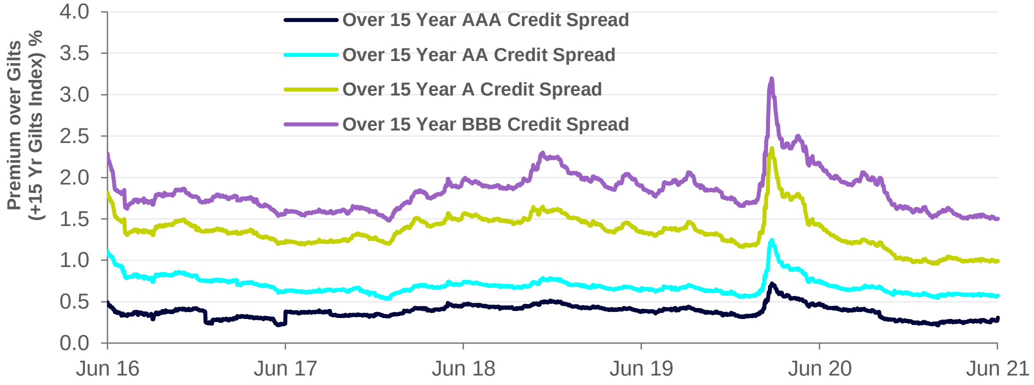
- Real gilt yields remain negative for all maturities.
- Real yields fell slightly across all maturities, except 5 years, and are still at similar levels to last quarter across most of the curve.

Corporate bond spreads largely unchanged over the quarter

Figure 8: GBP corporate bond spreads over gilts by rating (change over month/quarter/year)

Source: Bloomberg, Bank of America Merrill Lynch, Capita

Figure 9: GBP corporate bond spreads over gilts by rating (historic)



Source: Bloomberg, Bank of America Merrill Lynch, Capita

Asset class performance summary in local currency and GBP

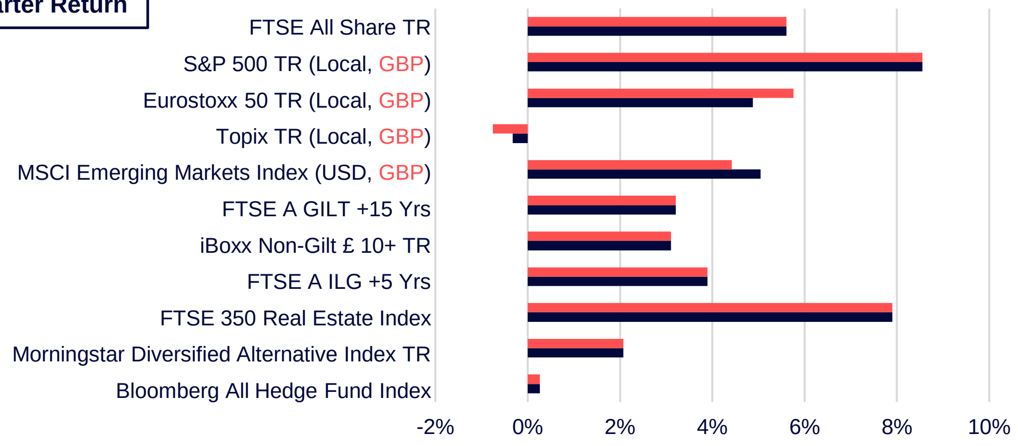
Asset class performance summary

- The charts below and the table to the right show the one-quarter and one-year performance in local currency and GBP of investments in major asset classes to the end of June 2021.
- Over the quarter, US equities was the best performing asset class.

Asset Class	Quarter Return	1 Year Return
FTSE All Share TR	5.6%	21.5%
S&P 500 TR (Local, GBP)	8.5%, 8.5%	40.8%, 26.3%
Eurostoxx 50 TR (Local, GBP)	4.9%, 5.8%	28.2%, 21.2%
Topix TR (Local, GBP)	-0.3%, -0.8%	27.3%, 10.9%
MSCI Emerging Markets Index TR (USD, GBP)	5.0%, 4.4%	40.9%, 23.9%
FTSE A GILT +15 Yrs	3.2%	-10.9%
iBoxx Non-Gilt £ 10+ TR	3.1%	0.7%
FTSE A ILG +5 Yrs	3.9%	-4.4%
FTSE 350 Real Estate Index	7.9%	21.2%
Morningstar Diversified Alternative Index TR	2.1%	2.8%
Bloomberg All Hedge Fund Index	0.3%	6.3%

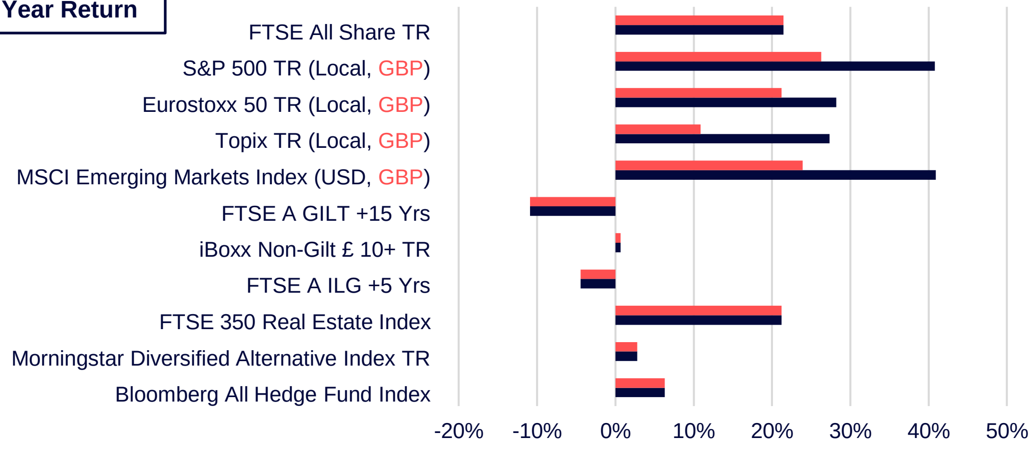
Total returns in local currency, GBP | Source: Bloomberg, Capita

Quarter Return



Source: Bloomberg, Capita

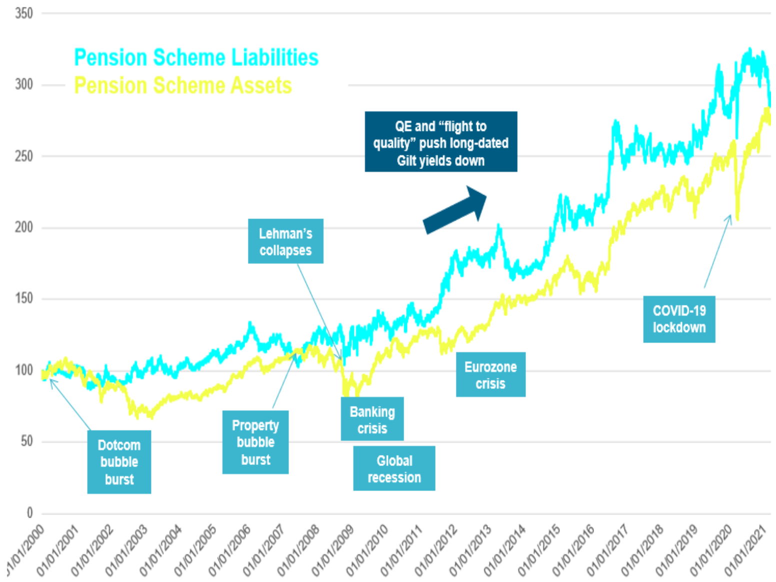
1 Year Return



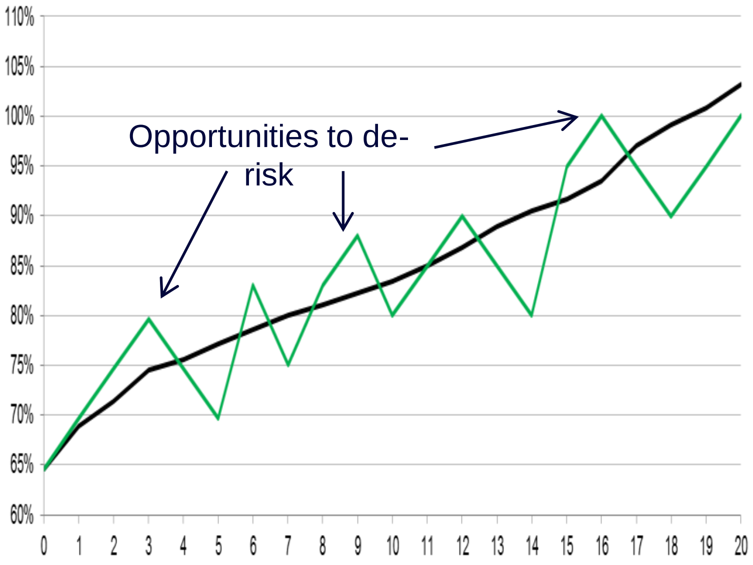
Source: Bloomberg, Capita

An introduction to dynamic de-risking triggers

Some schemes have missed short-lived opportunities when assets and liabilities have moved close together



Schemes invested in equities experience funding level outcomes which differ from projections



Monitoring with intent

- Introducing a dynamic de-risking framework will try to **make sure that de-risking takes places at the optimal times** in a pension scheme's journey, rather than being reviewed triennially.
- In conjunction with the scheme actuary, we can **monitor** a scheme's funding level and risks **daily** using the PFaroe technology.
- We can implement a **trigger based de-risking framework**, **which takes risk off** by moving from growth assets to matching **only as the funding position improves**, based on a funding-level information feed. Triggers are monitored daily.
- We can also provide quarterly monitoring reports which show the position of a scheme versus the agreed triggers.

Dynamic de-risking triggers – case study

A client of £19.5m in assets and approximately 650 members wanted to look at a dynamic trigger mechanism.

We performed the initial analysis to set up triggers based on the 2011 actuarial valuation. The trigger plan was agreed in 2012. At that point, the solvency level was approximately 60%.

We agreed a series of 8 triggers to get to fully funded on a low risk basis by 2021. The aim was to then move to 100% in gilts. This was revised later on as buyout came within range to be an approximate portfolio to better match annuity prices.

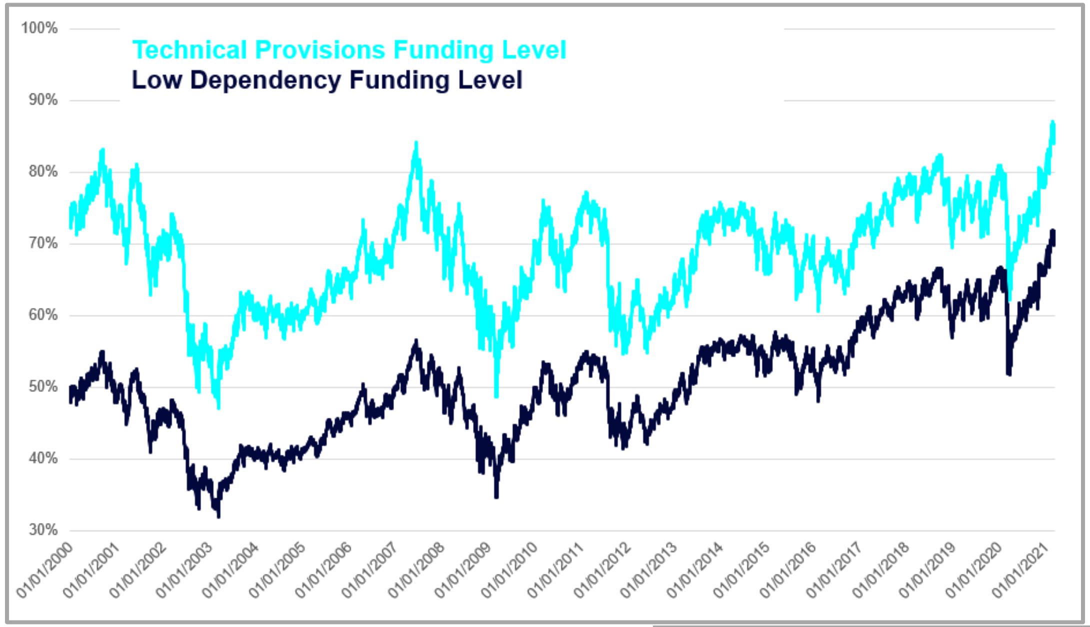
Between 2013 and 2016 a number of triggers were hit. We then produced revised analysis following a new actuarial valuation, which allowed us to reset triggers, with only 3 triggers remaining – still with the aim of targeting full-funding on a low risk basis by 2021.

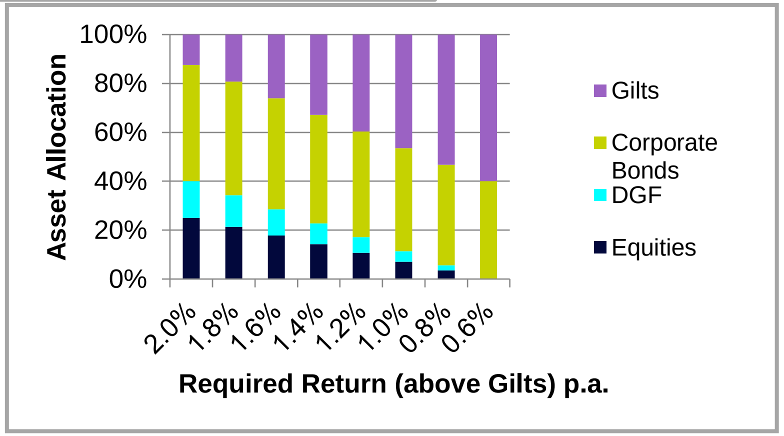
In 2018 the final trigger was hit and buyout was within reach. Improvements in funding then allowed the plan to buy out completely in 2020, with the final assets being transferred to an annuity provider.

"We have been using Capita's daily de-risking trigger service for over five years. Our scheme has three sections and in 2020 we were able to purchase annuities for all the liabilities in one section of the scheme due to the de-risking actions we had taken. The trigger framework is clear and when a trigger is hit, advice is given by the investment consultant with the confirmation of the scheme actuary.

This gives us the comfort to act and implement the pre-agreed investment switches. The other two sections remain on triggers and both are close to their next trigger. The service gives us confidence that if a short term market event leads to an unexpected improvement in funding, we are ready to act."

Chair of Trustees





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Regulatory statement

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The information provided is based on our understanding of current law and taxation as at the date of this report.
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