Investment Update

The LCP Monthly Brief – September 2022

LCP INSIGHT CLARITY ADVICE

Equities

Volatile market conditions resulted in equity markets falling sharply by 7.1% (in € terms) in September. The US dollar continued to strengthen against the Euro, providing some protection against the large loses experienced by Euro investors.

Higher than expected inflation expectations, government budget announcements and rising interest rates were key drivers of negative returns and difficult market conditions which challenged investors. Recession risk has remained a key headline as central banks grapple with difficult decisions between trying to tame inflation while limiting the impact on growth.

Governments released plans for support packages to curb high energy bills for consumers along with additional measures to aid the increased living costs. However, fear continued to build with concerns that these measures will not be enough to combat the energy crisis which continued to escalate over the month.

Bonds

Long-dated core Eurozone bond prices fell 8.5% over the month, with the yield on the AAA Eurozone 15+ Year Index rising by 0.5% to 2.2% by month-end. Prices fell by 7.1% on the Euro Broad Sovereign 10+ Year Index, with its yield rising by 0.5% to 3.1% by the end of September.

Bond markets faced turbulent conditions following the announcement of the UK's "mini-budget" which resulted in the Bank of England (BoE) having to step in to stabilise the market by implementing a time limited bond-buying programme. Eurozone inflation continued to persist at elevated levels, recording a new record level of 10% over September. The European Central Bank (ECB) raised base rates to 0.75% p.a. with further increases expected at the next ECB meeting in October.

Sample DB Scheme

The funding level of our sample DB scheme decreased to 97.8% as its assets fell by more than its liabilities (calculated using an MFS proxy) over September.

Sample DC Schemes

Our three sample DC Strategies all fell as most asset classes were negative for the month.

All returns are in € terms	Sept '22 %	3 Months %	Year to Date %	1 Year %	3 Years % pa	5 Years % pa	10 Years % pa
Equities							
FTSE World	-7.1	-0.1	-13.2	-5.0	8.5	9.4	11.2
FTSE World (€ Hedged)	-8.3	-4.8	-21.2	-15.7	5.7	6.3	9.5
FTSE Eurozone	-6.4	-4.8	-22.1	-17.8	0.2	1.2	n/a
FTSE World ex Eurozone	-7.1	0.3	-12.3	-3.7	9.3	10.3	11.6
FTSE North America	-6.8	1.5	-12.3	-1.7	11.8	13.1	14.2
FTSE Emerging Markets	-8.2	-4.1	-11.2	-10.3	3.3	3.7	4.9
Bonds							
Euro Sovereign AAA (15+ yr)	-8.5	-8.6	-32.1	-30.9	-13.4	-3.6	1.1
Euro Broad Sovereign (10+ yr)	-7.1	-8.6	-29.5	-29.9	-11.8	-2.7	2.6
Euro Inflation Linked	-6.2	-6.5	-17.2	-17.2	-4.7	-1.8	0.7
Euro Corporate (5+ yr)	-5.1	-4.5	-22.0	-22.7	-7.5	-2.7	1.2
Other							
Commodities	-7.8	-10.3	21.8	23.6	12.2	7.8	-3.9
Fund of Hedge Funds	0.0	1.0	0.8	1.8	5.9	4.7	4.4
€/$	-2.5	-6.5	-13.8	-15.3	-3.5	-3.7	-2.7
€/£	1.5	1.9	4.3	2.1	-0.4	-0.1	1.0

Bond Index Yields	31 Aug '22 %	30 Sep '22 %	Change (b.p.) %
iBoxx Euro Sovereign AAA (15+ yr)	1.71	2.22	0.51
iBoxx Euro Broad Sovereign (10+ yr)	2.62	3.14	0.52
iBoxx Euro Corporates (5+ yr)	3.68	4.45	0.77

Sample Pension Schemes	Sept '22 %	3 Months %	Year to Date %	1 Year %	3 Years % pa	5 Years % pa
DB Schemes						
Assets	-6.8	-3.5	-20.2	-16.0	-1.6	3.2
Liabilities	-2.4	-1.7	-9.9	-8.3	-1.2	3.0
Change in Funding Level	-4.5	-1.9	-11.4	-8.4	-0.4	0.2
DC Schemes						
High Risk Strategy	-4.9	-0.8	-11.7	-6.6	4.4	5.3
Medium Risk Strategy	-6.0	-2.9	-17.8	-13.8	-0.6	3.2
Pension Purchase Strategy	-6.2	-5.9	-24.6	-23.6	-10.0	-2.6

Sources: LCP, Bloomberg, Reuters, MarketWatch, FT, Markit and iBoxx

Investment Update

Market Performance – Q3 2022

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Background

Global equity markets fell 0.1% (in € terms) in Q3 2022. Market conditions remained highly volatile over the quarter. Inflation and interest rates continued to rise alongside increased recessionary risk which resulted in a challenging environment for investors and policy makers.

Longer-dated Eurozone government AAA-rated bond prices fell by 8.6% (as yields rose) over the quarter. Central banks began or continued to implement interest rate rises with the ECB raising rates to 0.75% p.a. (the highest level since 2011).

Equity Performance

July: Global equity markets rose 10.3% in July (in € terms), the highest monthly performance since 2020. The strong market returns reversed some of the sharp losses experienced in the first half of the year. One of the main drivers was a fall in interest rate expectations. Several large technology firms such as Microsoft and Apple released stronger than expected earnings which also contributed to the market returns.

Pent up tourism demand helped the Eurozone performed strongly this summer by contributed to stronger than expected GDP growth. Eurozone inflation continued to climb reaching a new high of 8.9% in July. The continuation of the Russian invasion of Ukraine and post pandemic disruptions remained major issues for the Eurozone with the outlook of a recession still posed as a high risk.

August: Following a ~10% recovery in July, global equity markets fell 2.6% in August (in € terms). The US dollar continued to strengthen against the Euro, providing some insulation from falling equity markets for unhedged Euro investors. Market performance was mixed over the month with initial strong gains following lower than anticipated US inflation data.

Hawkish comments from the US Federal Reserve caused markets to fall sharply in the last week of August, as the Federal Reserve signalled its commitment to raising interest rates in the battle against inflation. Technology and growth stock valuations were impacted most due to their sensitivity to interest rate rises.

The energy crisis in Europe intensified as Russia announced at the end of month the suspension of the flow of gas through the Nord Stream pipeline. Fears escalated that Russia will “weaponise” energy supplies to Europe in retaliation to the continued sanctions implemented on them since they invaded Ukraine.

September: Volatile market conditions resulted in equity markets falling sharply by 7.1% (in € terms) in September. The US dollar continued to strengthen against the Euro, providing some protection against the large loses experienced by Euro investors.

Higher than expected inflation expectations, government budget announcements and rising interest rates were key drivers of negative returns and difficult market conditions which challenged investors. Recession risk has remained a key headline as central banks grapple with difficult decisions between trying to tame inflation while limiting the impact on growth.

Governments released plans for support packages to curb high energy bills for consumers along with additional measures to aid the increased living costs. However, fear continued to build with concerns that these measures will not be enough to combat the energy crisis which continued to escalate over the month.

Bond Performance

Eurozone bond yields fell over **July**, the first monthly fall in yields since November ’21. The ECB made its first interest rate rise of 50bps which resulted in a move out of negative interest rate territory for the first time in 8 years. The ECB face many challenges ahead due to inflation and political uncertainty following the Italian Prime Minister’s resignation during the month. To help the resilience of bond markets in periphery countries such as Italy, Spain and Portugal who have higher interest rates, the ECB announced a new monetary tool called the Transmission Protection Instrument (TPI). This will allow the ECB to purchase Italian debt over German debt, as an example, to help control the interest rate differential and maintain stability across the Euro area.

Inflation continued to rise during **August**, with Eurozone inflation hitting a new record of 9.1%. Central bankers continued to face challenging market conditions in their attempts to combat inflationary pressures alongside increased recession risk. Market participants were watching the ECB with interest as they decide on increasing Eurozone interest rates further.

Bond markets faced turbulent conditions in **September** following the announcement of the UK’s “mini-budget” which resulted in the Bank of England (BoE) having to step in to stabilise the market by implementing a time limited bond-buying programme. Eurozone inflation continued to persist at elevated levels, recording a new record level of 10% over September. The European Central Bank (ECB) raised base rates to 0.75% p.a. with further increases expected at the next ECB meeting in October.

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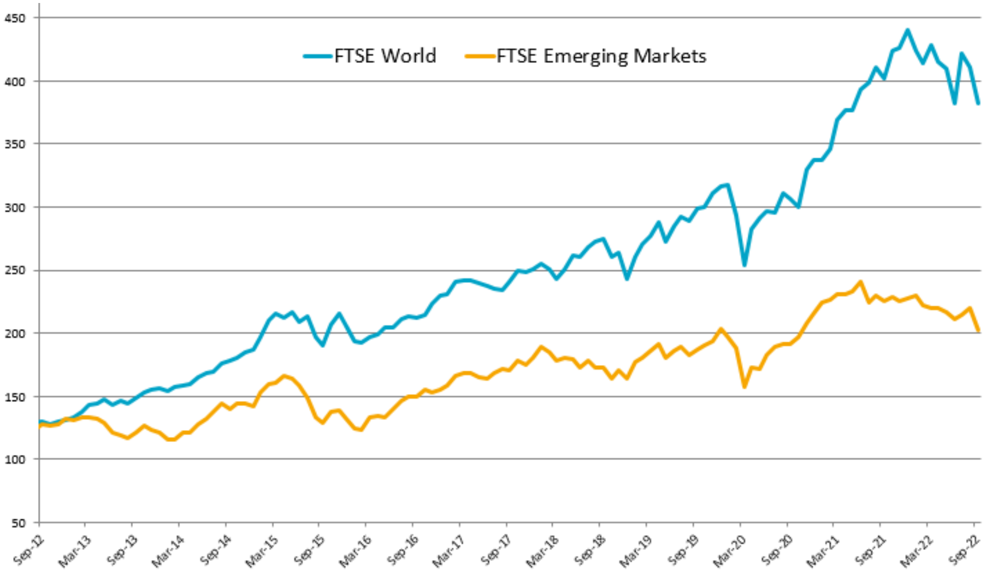
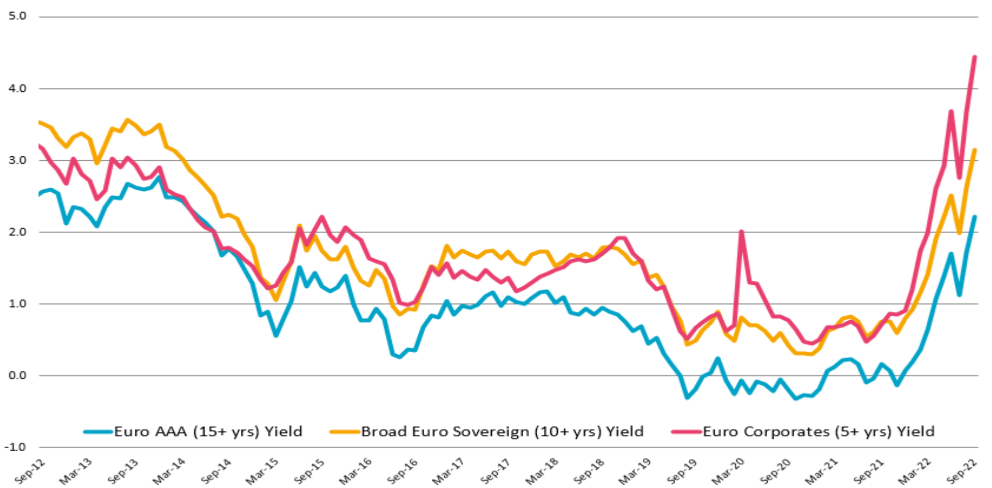
Equity Market Performance



Sample DB Funding Level Progression (MFS proxy basis)

Historical Bond Yields



Sample DC Scheme Performance