

June 2018

Dear Member,

Hermes Group Pension Scheme: Annual Newsletter

This is the third newsletter of the Hermes Group Pension Scheme.

This issue of the newsletter covers:

- Member Nominated Trustee Director process
- Update on sponsoring employer
- Triennial actuarial valuation as at 31 December 2017 – progress report
- Report and Accounts - 31 December 2017
- Investment Strategy and Investment Performance
- Membership Update
- Governance Update
- General pensions news
- FAQs and Contact Information

The Trustee is happy to receive any feedback you may have on the newsletter and encourages any comments or suggestions to be forwarded to the Scheme Secretary.

The Trustee of the Hermes Group Pension Scheme

Member Nominated Trustee Director Process

Douglas Bradford's first term of office as a Member-Nominated Trustee Director (MNTD) is due to expire in September 2018. Douglas is intending to stand for re-election. The Trustee Board, along with the Sponsoring Employer, is therefore asking for nominations from other Scheme members for this position. More information on the role of a Trustee Director and the nomination process is included in a separate letter enclosed with this Newsletter.

Update on sponsoring employer

The Trustee agreed in December 2017 to remove Hermes Fund Managers Limited (HFML) as a sponsoring employer of the Scheme, leaving BT Pension Scheme Trustee Limited (BTPSTL) as the sole sponsoring employer.

There were various positive outcomes for the Scheme which resulted from this. A payment was made by Hermes into the Scheme, as detailed in the Trustee Report & Accounts, which was estimated as having eliminated the Scheme's funding deficit on a Technical Provisions basis at that time, and allowed the Trustee to undertake further derisking of the portfolio of assets. It also paved the way for a new era in the relationship between the Trustee and BTPSTL.

An announcement of the removal of HFML as an employer was made in our letter to you in January 2018. The Trustee hopes that the letter sent to you in January this year, the detail in the Trustee Report & Accounts, and a 'Questions & Answers' document which has now been posted on the member website, will together provide sufficient information about the agreement to remove HFML as a sponsoring employer of the Scheme.

Members may have seen a subsequent announcement in the press in relation to the sale of a majority stake in HFML to Federated Investors. Please be assured that the Federated Investors transaction will have no impact on the pension benefits provided to you from the Scheme or the security of those benefits which continue to be supported by BTPSTL following the removal of HFML as a sponsoring employer of the Scheme.

Triennial actuarial valuation as at 31 December 2017 – progress report

The results of the last formal triennial Actuarial Valuation as at 31 December 2014 are shown below. Between formal triennial formal valuations, the Scheme Actuary rolls forward calculations each year in 'Annual Funding Updates' and the results of these calculations are also shown below.

	31/12/2014	31/12/2015	31/12/2016
Liabilities	£170.7m	£175.3m	£203.8m
Assets	£138.6m	£144.0m	£181.1m
Deficit	£32.1m	£31.3m	£22.7m
Funding Level	81%	82%	89%

The next full actuarial valuation is as at 31 December 2017. The Trustee reviewed the preliminary assumptions to be used in the valuation of the Scheme liabilities when it met in March 2018. The Scheme Actuary will present initial results of the valuation to the Trustee when it meets in June 2018. Negotiations on final assumptions and results will take place between the Trustee and BTPSTL in the latter half of 2018.

Report and Accounts – 31 December 2017

The Trustee Report and Accounts for the year ending 31 December 2017 is available on the front page of the HGPS member website:

<https://www.hermes-investment.com/hgps/wp-content/uploads/sites/99/2018/05/hgps-accounts-2017.pdf>

If you would like to have a printed copy of the Report and Accounts, you can print them directly from the Scheme website; otherwise please contact the Scheme Secretary at the address listed at the end of this newsletter.

The Accounts show that the value of Scheme assets at the start of the accounting period, 31/12/2016 was £181m. During the year, income to the Scheme from contributions was £42m, asset values moved up £20m, outgo to members was £9m. This resulted in a value of Scheme assets at the end of the year, 31/12/2017, including cash at bank, of £234m.

Investment Strategy

The Scheme Statement of Investment Principles (SIP) was updated in March 2017. Following this, over the course of the remainder of 2017, various initiatives were made.

Over the summer of 2017 it was agreed to hedge 50% of our exposure to foreign currency on developed market equity. Currency-hedged versions of LGIM's world developed equity and RAFI funds were set up and a 50% allocation made to them out of their currency-unhedged equivalents. This derisks the Scheme's portfolio of assets to an extent.

It was agreed that hedging levels of interest rates and inflation rates should increase to 100% of assets, and an Investment Implementation Committee was set up to move the position to 100% over a period of 18 months to January 2019. To facilitate this, the LDI portfolio was moved to a QIAIF arrangement towards the end of the year. The QIAIF (Qualifying Investor Alternative Investor Fund) is an Irish-domiciled bespoke pooled fund managed by Legal & General Investment Management (LGIM), in which the Scheme is the only investor. The advantages of the QIAIF are that we can hold a wider variety of assets to achieve our desired level and shape of hedging and meet the collateral requirements, and overall the costs are lower than using LGIM's standard range of pooled funds for hedging. This derisks the Scheme's funding position as it allows the value of the assets and the value of the liabilities to move up and down in tandem as interest rates and inflation rates move.

The additional payment made as part of the agreement to removing Hermes as a sponsoring employer allowed the Trustee to further derisk assets by reducing the allocation to equities, and a revised SIP has been agreed in the first half of 2018 to reflect the initiatives made as well as a revised target asset allocation. The SIP is available to view on the member website, in the Scheme Overview section.

Investment Performance – year ending 31 December 2017

Over the year the overall investment return for HGPS was 11.0% against the benchmark return of 8.3%. The Scheme's performance in the last five years is shown in the table below:

Comparison with benchmark 2013 – 2017						
Annual Rate of Return %	2013	2014	2015	2016	2017	2013 to 2017 Annualised
HGPS	9.7	12.6	3.0	24.3	11.0	11.9
Benchmark	7.9	13.2	4.5	23.2	8.3	11.2
HGPS out/(under) performance of benchmark*	1.8	-0.6	-1.5	1.1	2.7	0.7

*the differences in this table are based on an arithmetic approach

Over the five-year period from 2013 to 2017, the Scheme returned 11.9% per annum, outperforming its benchmark return over the period. For background, over the year to 31 December 2017, the Consumer Prices Index rose by a modest amount (2.9%).

How is the Scheme Benchmark calculated?

For most of the conventional assets, such as equities and corporate bonds, the benchmark used is a relevant market index. For other asset classes, such as multi-asset and diversified credit, the benchmark is measured against a cash return plus a margin. Performance against these kinds of benchmarks can be quite volatile over the short term as the managers do not actively track them. The Liability Driven Investment (LDI) portfolio references liability values which are tracked, and calculated based on gilt yields.

The Scheme Benchmark is a weighted average of the individual benchmarks explained above. It is not appropriate to compare the Scheme with its peer group due to the individual circumstances that apply to each pension scheme (such as different maturity profiles and the amount of investment risk taken).

The Trustee also monitors the asset performance against the movement in the actuarial value placed on the Scheme's liabilities, in other words, the progress of the funding level.

Membership Update

The figures and chart below show the history of membership from 2006.

	31.12.2008	31.12.2011	31.12.2014	31.12.2017
Employed deferred	306	151	80	52
Deferred	258	361	400	369
Pensioner	81	115	140	180
Total	645	627	620	601



Governance Update

Over the course of the year there have been various changes made to the Trustee Board. Carol Woodley stepped down as Chair and Trustee at the end of her term of office and was replaced by PTL, represented by Alison Bostock. David Bridges' term of office also ended and he was replaced by Alan Ormrod following an MNTD election over the summer.

Trustee Board		
PTL represented by Alison Bostock	Independent Chairman	Appointed 12 October 2017
Douglas Bradford	Member Nominated	Appointed 18 September 2014
Alan Ormrod	Member Nominated	Appointed 22 September 2017
Ingrid Kirby	Employer Nominated	Re-appointed 1 September 2017
Matt Simms	Employer Nominated	Re-appointed 23 September 2017

Advisers were unchanged over the course of the year. However, with the finalisation of the Trustee Report & Accounts, and with BTPSTL as the sole sponsoring employer with BTPS having a 30 June year end, it has been agreed to move the year end for the HGPS accounts to 30 June and to change auditors to KPMG, as used by BTPS, to benefit from synergies.

Advisers		
Secretary	Inside Pensions Limited	Rachael Fortescue John Dutton
Lawyer	Sackers & Partners LLP	Pauline Sibbit
Covenant Adviser	Lincoln	Alex Hutton-Mills
Investment Adviser	Hymans Robertson LLP	John Walbaum Russell Chapman Beenesh Googoolye
Actuary	Willis Towers Watson Limited	Emma Palfreyman
Administrator / Pensioner Payroll / Accounting	Capita Employee Benefits Limited	Phil Hunter Adam Luscombe Warren Swales
Auditor	Deloitte LLP [to May 2018]	Bob Cooper

The Trustee Board is aware that Capita is working through a transformation plan, and has sought, and received, assurances from Capita regarding their business proposition. Capita attend quarterly Trustee meetings to present their Administration Report for the most recent quarter. The Trustee continues to monitor the position carefully, and update its Business Continuity Plan as appropriate.

General pensions news

General Data Protection Regulation

The EU General Data Protection Regulation (GDPR) replaces the Data Protection Directive 95/46/EC and is designed to harmonise data privacy laws across Europe, to protect and empower all EU citizens' data privacy and to reshape the way organisations across the region approach data privacy. The legislation became effective as at 25 May 2018.

The Trustee has reviewed guidance from Sackers as legal advisers to the Scheme and has undertaken a project to ensure compliance with the regulations as at May 2018 and ongoing.

The Trustee needs to hold personal data about members in order to calculate and pay benefits. More detail about how and why we do this has been set out in an updated privacy notice, which was issued to all members by post in May 2018, and which was also posted on the member website, on the front page.

More information is available here:

www.eugdpr.org

<https://ico.org.uk/for-organisations/guide-to-the-general-data-protection-regulation-gdpr/>

White Paper

The DWP has published a White Paper: "Protecting Defined Benefit Pension Schemes". This paper explains how the government intends to increase the protections for defined benefit scheme members and make improvements to the system. This includes government plans to protect private pensions through a stronger Pensions Regulator, as well as clarify scheme funding principles.

More information is available here:

<https://www.gov.uk/government/publications/protecting-defined-benefit-pension-schemes>

FAQs and Contact Information

The Trustee would like to provide you with the opportunity to ask any questions you may have in relation to the Scheme. If you have any queries on the content provided within this newsletter, please contact the Scheme Secretary via any of the following:



hermes@insidepensions.com



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Should you need any details on your pension benefits, or if your personal circumstances have changed, please contact Capita Employee Benefits, the Scheme Administrators via any of the following:



hermes.pensions@capita.co.uk



01227 771445



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