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Unit Linked & With-Profits Pension Funds Investment Report 2019

Market Commentary

Global Overview

Global equity markets powered ahead, with US and European stocks performing particularly well. Shares in Japanese and UK companies were relative laggards, but still made double-digit gains. Political and economic issues were to the fore, ranging from Brexit to the trade dispute between the US and China.

Shares got off to a good start in 2019, supported by a more favourable interest rate outlook and strong corporate profits. There was a hiatus in the month of May, with many markets tumbling on renewed fears about trade relations. In the UK, Prime Minister Theresa May announced her resignation. She was replaced by Boris Johnson.

The Federal Reserve (Fed) moved to lower US interest rates. It cut the main rate three times – in July, September and October. The European Central Bank (ECB) also trimmed rates and announced bold new measures aimed at reviving the beleaguered Eurozone economy. Latterly, political developments dominated headlines. The US Democratic Party moved to impeach President Trump. Meanwhile, in the UK, the parliamentary furore over Brexit intensified and a general election was called for 12 December.

Stocks ended the year on a high, with investors encouraged by a positive turn of events in the US-China trade saga. Some encouraging economic data from around the globe also helped to propel share prices higher in the final days of 2019.

UK

UK share prices moved higher. However, despite double-digit gains on the two main indices, they were outpaced by several other developed markets. The stock market had to weather political upheaval and Brexit-related uncertainty. At several points, sterling weakness benefited companies that make the bulk of their earnings overseas. At the sector level, shares in technology and industrials companies performed particularly well. By contrast, oil & gas and telecoms shares disappointed.

Although UK equities performed well in the early months of 2019, they fell once again in May. Prime Minister Theresa May announced her resignation as MPs once more moved to reject her European Union Withdrawal Agreement. Her successor, Boris Johnson, ejected most of the previous cabinet and appointed fellow pro-leave supporters in their stead. The political twists and turns period culminated in a three-month extension to Brexit, the approval in principle of Mr Johnson's Withdrawal Act and the UK parliament voting in favour of a snap election. The Conservative Party won a conclusive victory in the vote, which took place in December. The election result sparked a relief rally in the UK stock market. In particular, the share prices of domestically-focused companies rose sharply.

In other news, Andrew Bailey was announced as the new Bank of England (BoE) governor. The residential property market was boosted by mortgage approvals in November hitting a near three-year high. Data released in December pointed to a rise in real wages to levels not seen since before the financial crisis over a decade ago. On top of this, UK economic growth for the third quarter was revised higher.

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Europe

European shares ended 2019 on a high, outperforming most other regions and producing strong gains during 2019. Concerns over rising inflation and higher interest rates were an initial worry for investors. The on-off US-China trade dispute also dominated investor sentiment, given that Europe's economies are export-dependent. In particular, the auto industry suffered. Economic growth in the Eurozone halved in the second quarter of 2019, rising just 0.2%.

There were worries that Germany could be teetering on the brink of recession. A contraction in the German economy, the biggest in Europe and the world's fourth-largest, had wider implications for global growth. After shrinking in the second quarter, Germany managed better-than-expected growth of 0.1% in the third quarter. Strength in the consumer-driven part of the domestic economy is helping to offset the beleaguered manufacturing sector. Confirmation that activity was picking up was demonstrated by improved business confidence surveys towards the end of the year. Nevertheless, its manufacturing industry continued to struggle.

Data from France and Spain was also worse than expected, reinforcing calls for the ECB to take urgent action. However, as with Germany, signs of stabilisation started to appear in late 2019. The mid-year weakness of the Eurozone economy eventually led to the ECB cutting interest rates and restarting its bond-buying programme in September. This then boosted shares in the Eurozone. The ECB lowered its deposit rate from -0.4% to -0.5%. Since June 2014, the institution has been charging banks to hold funds on deposit, rather than paying them interest. The thinking behind this policy is that European banks will be encouraged to lend more money, shoring up the region's economy by increasing spending. Outgoing ECB President Mario Draghi also told governments that they need to act quickly to stimulate economic growth. His replacement, Christine Lagarde, reassured investors with her confirmation that the bank's softer tone would continue.

Gains accelerated towards the year end on encouraging signs of improving industrial output in China, clarity on Brexit after a decisive UK election result, and a US-China trade agreement in the offing. This was underpinned by a continued corporate spending spree on acquisitions.

Asia Pacific

Asian equities were up in local currency terms. The US-China trade war, concerns about Chinese growth and global monetary policy exerted influence on sentiment, both positively and negatively. Having rumbled on for a while, tensions between the US and China intensified at the start of 2019, as each side announced further tit-for-tat tariffs. This had a knock-on impact for the wider region, with technology stocks bearing the brunt of the selling. However, markets climbed after the Fed said it was putting interest rate rises on hold. Hopes of a trade deal also emerged. Thereafter, the narrative became a familiar one. In May, President Trump slapped new tariffs on China, which responded in kind. Markets tumbled. In June, both sides agreed a truce at the G20 summit in Japan, and markets rallied.

As the period progressed, the world's central bankers lifted market sentiment. Most said they would act to support their respective economies by way of rate cuts and quantitative easing. This included China, which is facing its slowest growth in nearly 30 years. In politics, the re-election of incumbents in India and Indonesia were seen as positive for investors. Many believe the results will lead to further market-oriented reforms. Meanwhile, the Fed cut rates in July, September and October. As the period came to a close, the US and China agreed to sign a 'phase-one' trade agreement. This helped ensure that Asian equities finished on a high.

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Corporate Bonds
From early 2019, there were growing indications that the Fed was adopting a more dovish stance on monetary policy to forestall the effects of a global slowdown. While the ECB halted its quantitative easing (QE) programme in December 2018, a dovish tone from President Mario Draghi prompted markets to price in the prospect of further QE. Meanwhile, the prospect of further BoE interest rate hikes reduced amid mounting Brexit-related worries.

This led to a rally in risk assets, buoyed also by optimism around a US-China trade settlement. For the first three months of the year, corporate bond markets delivered strong returns. Returns were then flat in April, largely affected by Brexit uncertainties. In May, escalating global trade tensions came once more to the fore. Corporate bonds suffered as investors' appetite for risk fell, but recovered in June and July as market-friendly central bank policies led to a more constructive environment.

In the second half of the review period, returns from corporate bond markets were fuelled by falling government bond yields across developed markets and stable credit spreads in most higher-quality fixed income markets. Gilt yields rose in November and December, driven by improving global macroeconomic data. So, while spreads tightened, corporate bonds delivered a marginally negative total return. With the UK general election out of the way and the US and China seemingly close to a trade deal, uncertainty into the end of 2019 was reduced, helping market performance.

Government Bonds
While a shift in central bank policy from QE to quantitative tightening (QT) has been a feature of much of the past 12 months, the pendulum has now swung back towards monetary easing. At the beginning of 2019, government bonds had been bolstered by worries about higher-than-expected inflation, and the impact of protectionism on growth revived investors' appetite for risk-free assets. The Fed raised its target interest rate four times during 2018, but its primary message since the start of 2019 has been dovish. The Fed cut US interest rates at the end of July for the first time in more than 10 years, and again both in September and October. During December, however, it signalled that interest rates would be on hold for the foreseeable future. The ECB kept rates on hold until September, when it cut its deposit rate to -0.5% and announced the resumption of QE.

In the UK, Brexit negotiations continued to rumble on. Boris Johnson succeeded Theresa May as prime minister in July. While Johnson successfully agreed a deal with the European Union (EU), he was unsuccessful in securing UK parliamentary agreement. This led to a general election in mid-December, which resulted in an overwhelming victory for the governing Conservative Party. That was viewed by markets as positive; it removed the threat of renationalisation from some industries, and may allow the government to resolve the Brexit impasse. The feel good factor extended to 'safe' assets, and 10-year US Treasury yields moved higher. Germany continued its recent trend of weakening industrial and manufacturing data. In spite of this, 10-year German yields rose throughout December, ending the year as close to zero as they had been since July.

UK Commercial Real Estate
As expected, 2019 was a weaker year for real estate performance. According to the MSCI Monthly Index, full-year total returns are likely to be around 2%. This is significantly less than the 7.5% full-year number achieved in 2018. The monthly total return for November (the latest data available) was 0.1%, the weakest single month since July 2016.

Future return expectations look more tepid and investors are reducing their risks. They are also de-risking their real estate allocations in anticipation of lower economic growth forecasts. There was a strong appetite and competitive bidding for prime assets with long lease agreements in place. This underscores the level of demand currently chasing secure income streams. Investors are tending to avoid risk, with secondary assets and large vacancies proving to be out of favour.

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Properties with looming capital expenditure requirements, development risk and tenancy turnover are also being shunned by the discerning investor.

Overall, transaction volumes have been weaker. The exception has been the alternatives sector, where a small number of portfolio deals have propped up liquidity. Investors still like the stable, secure income this sector can offer. That said, the retail sector is at the other extreme of the spectrum, with activity now at a 10-year low. Market liquidity is thin and deal timeframes are being extended as opportunism creeps in. Some investors are trying to translate capital declines into bargain buying opportunities by renegotiating previously agreed sale prices downwards. This has put further pressure on valuations.

There is still a pronounced undersupply of logistics/industrial assets in the South East. This is driving strong rental growth and continued investor appetite for prime assets in well-connected locations. However, investor appetite seems to be weaker in the rest of the UK, where a supply shortage is less pronounced.

Japan

Equities in Japan delivered a positive return in yen terms. However, the period was characterised by many ups and downs, particularly around trade and the yen. Central banks, including the Bank of Japan, played their part, acting to support economic growth. A rush of foreign investors into Japanese stocks in October and November was also a positive driver.

Trade tensions were high at the beginning of 2019, and the yen was strong thanks to its ‘safe-haven’ status. This hampered a number of companies that sell goods overseas. However, the US Fed surprised investors in January when it said it would halt interest rate rises. Hopes of a breakthrough between the US and China were also positive.

Japanese equities surrendered all the gains they made in 2018 in the first four months of 2019. However, markets rebounded in June after the US and China agreed a truce, before tumbling in July and August when relations soured once more. Meanwhile, the Fed cut interest rates in July, September and October. Deterioration in Japan’s trade relations with South Korea was offset by better-than-forecast second-quarter GDP growth of 1.8%.

Analysts had pencilled in an annualised rate of 0.4%. At the close of 2019, hopes of further stimulus measures boosted Japanese share prices. A senior minister confirmed the government is looking to launch a 13 trillion yen (US$119 billion) spending package to bolster the economy.

US

US share prices had an outstanding 12 months, recording the best annual return since 2013. Before that, one would have to go back to the mid- to late-1990s to see a similar return.

During 2018, share price performance was weak. This partly was in reaction to the Fed’s determination to tighten monetary policy. The US-China trade dispute also detracted, particularly in the final quarter. In response, in early 2019 the US central bank softened its tone on interest rate hikes. This was the catalyst for a market recovery. Hopes that Washington and Beijing might resolve their trade dispute also boosted share prices. Events took a turn for the worse in May, however, as on-off negotiations on the subject collapsed.

In July, the Fed made its first rate cut since 2008, dropping the main US rate by 0.25%. Initially, investor reaction was mixed, as the Fed presented the cut as an adjustment rather than a change of policy. It made further reductions in September and October, however.

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Worries about global recession and trade frictions began to dominate investors' thoughts yet again. However, the prospect of renewed trade talks emerged in September, prompting a rally in equities after a dismal August. Towards the end of November, the S&P 500 Index hit a record high, boosted by the Fed's third rate cut of the year and a resilient third-quarter earnings season.

Merger & acquisition activity also helped propel shares higher, with the takeover of Tiffany by LVMH grabbing the headlines. There was also news of consolidation in the motor industry. Fiat Chrysler is to merge with France's Peugeot to create the world's fourth-biggest carmaker. This was underpinned by encouraging economic data, such as continued employment growth.

The year ended on an optimistic note, with positive signals from the Fed and a US-China trade agreement in the pipeline.

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Key Updates for Phoenix Life Limited
SPI With-Profits Fund Customers

Former Scottish Provident Limited 1 January 2020
Irish traditional with-profits pension policies

Your policy is part of the Phoenix Life Limited SPI With-Profits Fund (the 'with-profits fund').

Self Employed Deferred Annuity (SEDA) policies have guaranteed annuities / pensions.

Executive type pensions have cash sums at the selected retirement age that have been purchased with the premiums that have been and will be paid, and from previous bonuses we have added.

Bonus rates

We have reduced the annual bonus rates for Executive type pension policies. Annual bonuses for 2019 are 0% (was 0.5% for 2018).

We set annual bonus rates at a level that can be sustained by the investment returns we expect the fund to earn in the future. Any investment returns earned in excess of the annual bonus rate will be reflected in final bonus rates. We review annual bonus rates each year.

Annual bonus rates for SEDA pension policies remained at nil for 2019.

There has been no increase for SEDA policies because the benefits already guaranteed to be paid are high compared to the value of the underlying assets, and we are giving priority to paying a final bonus at the retirement date if at all possible. The addition of any future annual bonuses will depend on the future investment performance and experience of the with-profits fund, after allowing for the historic performance and the value of the guaranteed benefits.

We have reviewed our policy of concentrating on final bonuses before increasing annual bonuses and continue to believe that this is the fairest way for all policyholders to benefit from the returns of the with-profits fund.

We may add a final bonus on retirement at the selected retirement date. We do not guarantee final bonuses. We normally review final bonus rates twice a year from 1 January and 1 July. However we may change final bonus rates at any time.

Please remember that annual bonuses are only one part of the benefits from your with-profits policy. In many cases the benefits already guaranteed to be payable are very valuable and there may also be a final bonus. Please also remember that guarantees will normally be lost if your policy is surrendered or transferred out.

Investment approach

The with-profits fund consists of a wide range of assets with the aim of providing good growth potential over the medium to long term.

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On 31 December 2019, the split of assets for Irish traditional with-profits pension policies was approximately:

Company shares	22%	
Property	5%	
Other growth assets	3%	
Total growth assets		**30%**
Fixed interest stocks - issued by governments in the eurozone	47%	
Other fixed interest stocks - (including corporate bonds)	20%	
Cash	3%	
Total fixed interest and cash assets		**70%**
Total assets		**100%**

The investment return on the with-profits fund for these policies over the last few years is shown in the table below.

Phoenix Life Limited – SPI With-Profits Fund
Former Scottish Provident Limited
Irish traditional with-profits pension policies

Investment return
(before tax, expenses and charges)

Year	Investment return
2019	9%
2018	0.5%
2017	3%
2016	4%
2015	4%
2014	12%
2013	5%
2012	10%
2011	1%
2010	3%

We do not expect to make any changes to the investment strategy for the with-profits fund during 2020.

Surplus money

There is more money in the fund than we expect to pay out in claims. Some of this surplus money is used to protect the fund against unexpected shocks, for example a fall in the value of the fund's investments. However, the remainder can be released and used to increase the amounts we pay out to policyholders. From January 2020 this surplus is increasing policy payouts by up to 40.8% for those policies receiving a final bonus. The amount we are able to add to policy values will be regularly reviewed and may increase or decrease, and could even be removed entirely.

This information is correct at 1 January 2020.

If you have any questions or would like more information about your policy, please contact us. Our contact details are:

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Key Updates for Phoenix Life Limited
SPI With-Profits Fund Customers

Former Scottish Provident Limited 1 January 2020
Irish unitised with-profits pension policies

Your policy is part of the Phoenix Life Limited SPI With-Profits Fund ('the fund'). Your policy has with-profits units that have been purchased with the premiums you have paid. Some policies may be split between unit-linked funds and the with-profits fund. This information sheet refers only to the with-profits element.

Bonus rates
Annual bonuses from 1 April 2020:
- For all units purchased before 1 October 1999 (Irish pension series I) there is a guaranteed minimum annual bonus of 4.0% each year. We have continued to add this, but we have not been able to add any additional annual bonus.
- For the other series, where there is no guaranteed annual bonus, we have reduced the annual bonus at 4.5%.

We have reviewed our policy of concentrating on final bonuses before increasing annual bonuses and continue to believe that this is the fairest way for all policyholders to benefit from the returns of the fund.

The addition of any future annual bonuses will depend on the future investment performance and experience of the fund, after allowing for the historic performance and the value of the guaranteed benefits. Where series of units have a guaranteed amount of annual bonus, these will continue to be added as usual.

We are currently (as at 1 January 2020) adding a final bonus on retirement at the selected retirement date. However, we do not guarantee final bonuses. We normally review final bonus rates twice a year from 1 January and 1 July, but we may change the final bonus rates at any time. On surrender, transfer or retirement at any date other than the selected retirement date, we may apply a market value reduction. This would have the effect of firstly reducing any final bonus and then reducing the value of the units in the policy. We review the level of market value reductions regularly.

Investment approach
The fund consists of a wide range of assets with the aim of providing good growth potential over the medium to long term. On 31 December 2019, the split of assets for Irish unitised with-profits pension policies was approximately:

	Series I	Series II	Series III
Company shares	22%	44%	44%
Property	5%	10%	10%
Other growth assets	3%	5%	5%
Total growth assets	**30%**	**59%**	**59%**
Fixed interest stocks - issued by governments in the eurozone	47%	23%	23%
Other fixed interest stocks (including corporate bonds)	20%	13%	13%
Cash	3%	5%	5%
Total fixed interest and cash assets	**70%**	**41%**	**41%**
Total assets	**100%**	**100%**	**100%**

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The investment return on the fund for these with-profits units over the last few years is shown in the table below.

Phoenix Life Limited – SPI With-Profits Fund Former Scottish Provident Limited Irish unitised with-profits pension policies Investment return (before tax, expenses and charges)			
Year	Series I	Series II	Series III
2019	9%	14%	14%
2018	0.5%	-1.3%	-1.3%
2017	3%	7%	7%
2016	4%	3%	3%
2015	4%	8%	8%
2014	12%	14%	14%
2013	5%	11%	11%
2012	10%	11%	11%
2011	1%	-2%	-2%
2010	3%	6%	6%

We do not expect to make any changes to the investment strategy for the fund during 2020.

Surplus money

There is currently more money in the fund than we expect to pay out in claims. Some of this surplus money is used to protect the fund against unexpected shocks, for example a fall in the value of the fund's investments. However, the remainder can be released and used to increase the amounts we pay out to policyholders. From January 2020 this surplus is increasing policy payouts by up to 40.8% for those policies receiving a final bonus. The amount we are able to add to policy values will be regularly reviewed and may increase or decrease, and could even be removed entirely.

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Unit Linked Fund Returns for 2019

A. Ignis Asset Management:

Fund / Asset Class	2019
Guaranteed Deposit*	0.00%
Fixed Interest	2.11%
Cautious Managed	17.93%
Balanced Managed	24.13%
Adventurous Managed	28.45%
European Stock Market	25.57%
North American Stock Market	33.17%
World Stock Market	28.46%
UK Stock Market	31.75%
Far East Stock Market **	23.21%
Japan Stock Market	21.42%

www.ignisasset.com

* The bid price of this fund is guaranteed not to fall other than by the value of the annual reduction applied for the Irish Government tax levy.

** Please note that the Far Eastern Stock Market had exposure to the Japan Stock market

B. KBC Asset Management:

Fund /Asset Class	2019
Irish Equity	36.52%
Managed	17.93%
Euroland Equity	19.82%
Dividend Plus Global Equity (Top Picks)	20.81%
Dividend Plus Global Equity (Fallen Angels)	20.37%
Euro Balanced	27.80%
Balanced Managed	17.91%
Irish Stockmarket	37.23%

www.kbcam.com

C. BlackRock Investment Managers:

Fund /Asset Class	2019
Euro Global Balanced Managed	14.46%
Global Equity	34.65%
Euro Global Bond	3.13%

www.blackrock.co.uk/uksite/index.htm

D. Aberdeen Asset Management.

Fund / Asset Class	2019
Global Champions	25.94%
Technology	41.48%

www.aberdeen-asset.com

Source – Financial Express Analytics

Scottish Mutual International Limited (Company No. 242244) trading as Phoenix Ireland is regulated by the Central Bank of Ireland. Phoenix Life Limited, trading as Phoenix Ireland, is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority in the United Kingdom and is regulated by the Central Bank of Ireland for conduct of business rules. Scottish Mutual International Limited's registered office is 25-28 North Wall Quay, Dublin 1, Ireland. An up-to-date list of its directors, containing the particulars required by paragraphs (a), (b), and (c) of section 196(1) of the Companies Act 1963, is available upon request from the company's registered office. Phoenix Life Limited is incorporated in England (Company No. 1016269) and has a registered branch in Ireland (Branch No. 906073). Phoenix Life Limited's registered office is 1 Wythall Green Way, Wythall, Birmingham B47 6WG United Kingdom. Its directors are A B Davidson (UK), J P Evans (UK), M J Merrick (UK), A Moss (UK), M D Ross (UK), W Snow (UK), W R Treen (UK), S True (UK) and M N Urmston (UK).