DC COMMUNICATOR
Our experience. Your advantage.

March 2008
Issue 2

Property funds face liquidity issues

In this issue

WELCOME
to *DC Communicator*

"What a difference a day makes" – or in this case six months since the last *Communicator*. Markets were high, the economy was positive, prospective house buyers were complaining of bidding wars and (almost) no one had heard the term "sub-prime mortgage"!

In this issue, our feature article is very topical as it looks at property funds. A year ago everyone wanted to add a property fund to their range of DC choices. Now, faced with increasing liquidity issues, we have seen direct property funds putting constraints on their customers. This will have worried some members, which highlights the need for appropriate education. It will be interesting to see if members come out of property funds because they see unit prices falling or if they take the opportunity to invest when prices are lower than they have been. Does anyone else think that investors in financial markets are the only people who prefer to buy when prices are high rather than when they are low? Those who take a different approach tend to be called "counter cyclical" – and they are often the most renowned investors.

One of our other articles looks at corporate entertainment and asks for your views. Most businesses are about people and although many of us (perhaps most of us) are very busy doing our "stuff" – emails, meetings, the recurring duties of our roles and more emails – there is a lot to be gained from taking time out, relaxing and talking to your Relationship Director. Some great ideas and new solutions to old problems can be reached by talking and sharing experiences.

The purpose of *DC Communicator* is to look at topics that interest you, and I hope you find something you enjoy reading in this issue. Please let me know what you think of the newsletter and what you'd like to see in future issues.

Regards

Alan Salamon
Head of DC Client Management

Giving you the advantage

This year we will start rolling out our new client engagement offering – Corporate Advantage. We have developed Corporate Advantage to provide a range of relationship management services in one clearly defined wrapper. We hope this will help you increase your plan effectiveness, as well as assisting with employees' retirement planning.

The wrapper will include a comprehensive plan review, featuring participation and contribution level analysis. Your Relationship Director will work with you to identify any plan enhancements that could benefit either your company or your employees. They will then produce a business plan to help monitor progress against key improvement goals. You will also benefit from a regular service recap that will summarise the objectives previously agreed and highlight key accomplishments for the plan.

ADDITIONAL BENEFITS

Corporate Advantage will be offering insight and opinion on political, economic and demographic issues that may affect your business and your role as plan sponsor. This will include keeping you informed about new Fidelity products that may be of interest to your organisation and employees.

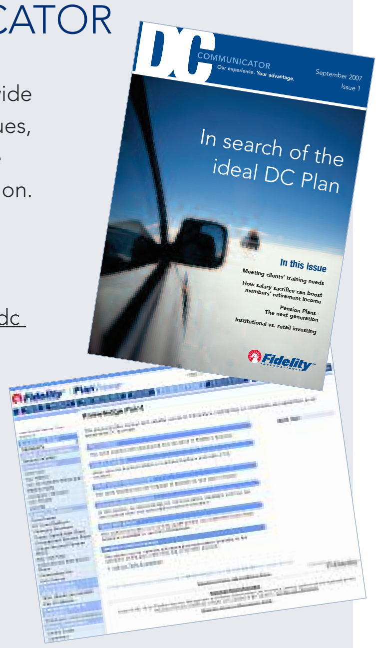
With more than ten years of industry-leading experience as a DC provider in the UK, and drawing on Fidelity's 40 years of DC experience in the US, we feel that Corporate Advantage gives plan sponsors the opportunity to take full advantage of the resources and expertise available at Fidelity.

Your Relationship Director will be in contact to discuss this with you.

ACCESS BACK ISSUES OF DC COMMUNICATOR

DC Communicator covers a wide range of news, topics and issues, many of which have relevance beyond their date of publication.

To catch up on previous issues simply go to www.fidelityinstitutional.com/dc Alternatively, log on to PlanViewer using your administrator user name and password and visit the *Knowledge Point* section. You'll find a link to *DC Communicator* in the left-hand menu.



Property funds face liquidity issues

For the last three to five years many of our clients and their advisers have been looking at how they can offer more diverse and sophisticated asset classes to members of their DC plans. Investing in commercial property is one way of achieving this diversification, as the returns show little correlation with those from equities and bonds. Here we give a brief introduction to commercial property and the issues that must be taken into account.

TYPES OF PROPERTY FUND

Property in DC plans refers to commercial property – it is important to highlight this as members' first instinct is often to think of residential property.

There are three main types of property fund available through DC plans:

- "bricks and mortar" funds that invest directly in properties such as offices, factories and shopping centres
- funds that buy shares in property companies
- funds that combine both of the above

Returns from all types of property fund are generated mainly from rental income and capital growth.

Another characteristic that all property funds share is their link to economic growth. With global growth estimates being revised down in 2008 and access to cheap borrowing drying up, the outlook for this asset class naturally becomes more clouded. There is, however, some positive news for the property sector when we look beyond Europe and the US – urbanisation and offshoring in Asia are increasing the demand for industrial and logistical properties, as well as retail space and hotels.

ISSUES OF LIQUIDITY

The commercial property market underperformed in 2007 and brought to the fore an important issue for DC members investing in bricks and mortar type funds – liquidity. This is not a new concern – UBS, for example, first closed its Triton Property Fund to new investment in 2005. However, it is really only in the past year that DC investors have been affected – bricks and mortar property funds from Standard Life, Threadneedle, Friends Provident and Aegon have all had liquidity concerns.

At the heart of this issue is the question of how the fund manager can meet redemption requests if there is little liquidity in the fund. DC plan members who are many years away from retirement may be able to accept that a pension investment is for the long term, and may therefore be willing to wait longer for sale proceeds. However, when people need quicker access to their money, liquidity may be a concern. Those affected could include investors who are trying to take benefits at retirement or who want to diversify as they near retirement. There may also be problems if death benefits need to be paid out quickly.

We know this is an issue for our clients and members as Fidelity has these types of property funds from both Standard Life and Threadneedle on our platform. It is unlikely that we will be able to offer further property options in the near future, as it is proving increasingly difficult to find bricks and mortar funds with adequate liquidity. We may simply have to accept that limited liquidity is an unavoidable characteristic of this type of property investment.

If the trend for diversification continues and property is to remain an investment option within DC plans, education is paramount. Members making investment choices must be encouraged to take account of the specific risks associated with this asset class, in addition to the usual risk considerations, such as volatility and inflation.

Better communications through technology

Technology has become an integral part of many people's lives. You can check emails on trains. You can record videos on mobile phones. You can manage bank accounts online. But where does retirement planning fit in?

We have a unique opportunity to encourage more effective retirement planning by using technology to make a pension plan accessible, easier to manage and more in line with other parts of their lives.

SO WHAT CAN FIDELITY OFFER?

Getting started

Employees can join your plan using our online enrolment system – a step-by-step process that takes them through the decisions they need to make. The system features plan-related documents, fund factsheets and online tools – such as *myPlan* and *What type of investor are you?* – which means employees have access to all the information they need.

Do your employees join through your own online or flex system? We can provide links to an information-only site for your plan directly from your system. This allows your employees to view the same information and tools available to members on PlanViewer.

Making progress

PlanViewer is a member's one-stop-shop for retirement planning – a form of "online banking" for your pension, with the same level of convenience. Yet our statistics show that PlanViewer is not the tool that members automatically use when they're looking for information or making decisions about their retirement planning. We can help you find creative opportunities to promote PlanViewer, in particular as part of other company initiatives. This also gives us an opportunity to promote retirement planning and the tools members have to help them.

Your company intranet can be used as an effective stage for promoting the plan as a company benefit and as the core of retirement planning. We can help ensure it offers members a direct link to PlanViewer.

Taking action

These are some simple examples of how we can use technology to communicate in ways that reach employees more effectively and are consistent with their other priorities. Fidelity's communication consultants can help you develop an approach that captures the power of technology to raise the profile of retirement planning at your organisation.

Recent Events

During 2007 we held a number of governance training sessions with a focus on DC investment. These were attended by many of our clients, and feedback showed they were a real success. In addition, some of you came to our golf day at Sunningdale, which offered a unique opportunity to discuss the issues facing scheme members, administrators and the industry in general. The format of playing 18 holes in the morning on the New Course and then – following an excellent lunch – 18 holes on the Old Course, proved a tough but enjoyable challenge for many guests, with some leaving late into the evening.

We are planning two more golf days this year – one for regular players and one for more occasional golfers. If you are interested in coming along, please let your Relationship Director know.

In past years our clients have also seen the Tate Britain's Turner collection at a private viewing and the Wallace Collection at an evening viewing.

For many people, particularly in the financial services industry, entertainment invitations have to be considered from a compliance perspective. This is something all employees at Fidelity need to bear in mind as well. We would be interested to know whether this affects your decision to attend events hosted by Fidelity and other service partners you may have. If there are any events you feel would be beneficial for sharing pension-related matters, please let your Relationship Director know.

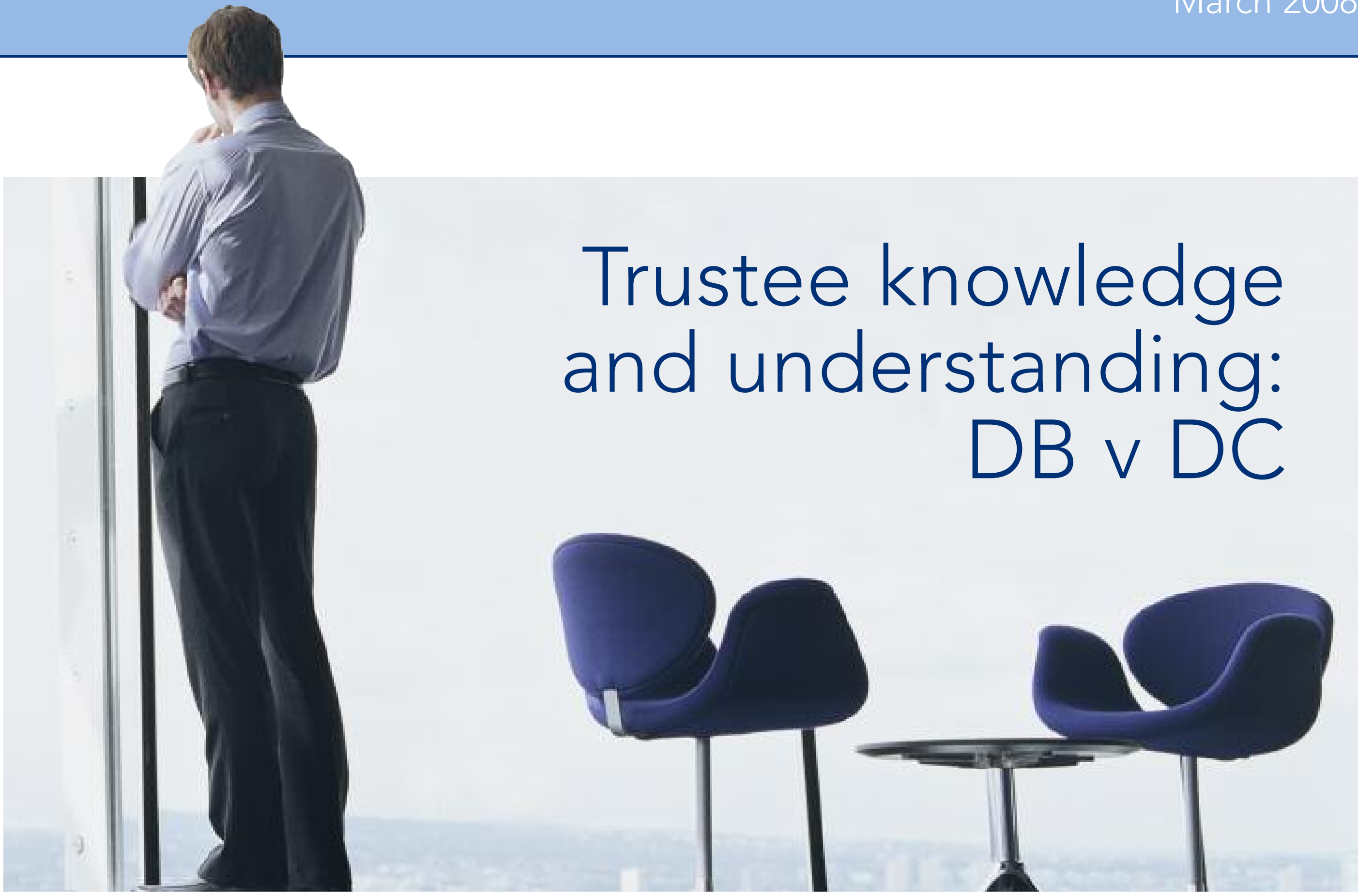
WHO'S WHO

Georgina Edwards

Georgina joined the Fidelity Client Management team a year ago and is an Associate of the Pensions Management Institute. She has seven years' pensions consulting experience in the UK and ten years of pension administration and consulting experience in South Africa. In her spare time, Georgie enjoys country walks and researching her family tree.

Martin Speakes

Martin joined Fidelity in April 2004, with over 25 years' experience in occupational and personal pensions. Before coming to Fidelity, Martin worked for Prudential Assurance and Guardian Employee Benefits. His hobbies include golf and keeping fit.



Trustee knowledge and understanding: DB v DC

Many trustees or governance board members of defined contribution schemes have come into the role having previously been trustees of defined benefit schemes. It is therefore understandable that they have approached the role in the same way – but is that really appropriate?

Since its establishment in April 2005, the Pensions Regulator has been developing extensive guidance and training for trustees and their advisers on a range of governance issues. They have produced codes of practice, other advice and a free e-learning programme for trustees – the "Trustee toolkit". Guidance has also recently been extended to cover all work-based pension arrangements – a move that has brought into focus the governance of contract-based schemes.

ESTABLISHING A FRAMEWORK

Under its regulatory code of practice No. 7, the regulator has set out a framework defining what trustees are expected to know and understand. Not surprisingly, there is a significant level of common ground between the requirements for defined benefits and defined contribution schemes. But the regulator has also drawn some clear distinctions between the two types of arrangements – to the extent that separate guidance has been developed for DB and DC. There are three main areas where distinctions have been made:

- The different types of assets available for investment and their characteristics. There is often a crossover between defined benefits and defined contributions in terms of investment strategy, though the application of this strategy often needs to be different. Defined benefit schemes have been moving towards a liability-driven approach and the risk/return trade off has led to diversification into alternative asset classes such as private equity, infrastructure and active currency management. But this has come at a cost of increased governance and, for some asset classes, a relative lack of liquidity, which would be inappropriate for DC.
- The principles relating to the funding of occupational DC arrangements and the risks taken on by members. A key difference between the two types of pension is the type of risk that members take on. For DB, members' risk is confined to the security of assets and the strength of the employer covenant. In a DC scheme the members are taking actual investment risk, which means they must understand the principles of accumulating a fund for retirement, the options for securing benefits and the risks they bear during their lifetime in the arrangement.
- The principles relating to the choice of investments. For DB schemes, investment strategies depend on existing levels of funding, projected future liabilities and expected cash outflow. These factors, together with the trustees' attitude to risk and an employer's tolerance to fluctuation in cost, determine the mix of assets. For DC, the approach taken is driven by the particular needs of the members. Key areas include the choice of an appropriate default option and the range of investment choices offered to members, which should balance the need for diversification with the members' ability to make appropriate choices.

KEEPING A FOCUS ON MEMBERS

The work of the regulator in increasing the knowledge of trustees and governance board members of defined contribution schemes is to be applauded. But we should not lose sight of the fact that the focus of all trustee and governance boards should be to help members achieve the best possible pension. Raising the board members' level of understanding will contribute little to that aim if insufficient emphasis is placed on conveying some of that knowledge to members.

Administration improvements

At Fidelity we are always looking to improve the service we offer our clients and plan members. An important aspect of this process is listening to your feedback and, when necessary, reviewing our approach. Two recent improvements we have introduced are changes to the transfer-in process and how we deal with the account of a member who dies.

A SMOOTHER TRANSFER-IN PROCESS

Experience tells us that many members are aware that transfers-in can take a long time – and even filling in the forms can be difficult. As a result, only about a third of transfer enquiries reach a successful conclusion, with the member's benefits moving to their new pension arrangement.

To address these challenges we have simplified and shortened both the transfer enquiry form and the application form from six pages to two. This makes them far less daunting, so members are more inclined to complete them rather than putting them to one side. We are also reviewing our standard letters to replace any jargon with plain English so that members receive clear and easily understandable communications throughout the transfer process.

These changes ensure that members always know exactly how a transfer is progressing. If there are delays, members will usually know who to contact to get things moving and, in our experience, most transferring schemes will respond more readily to a member than they will to the receiving scheme. A time-line flowchart, revised forms and other basic information will be available on PlanViewer.

SAFEGUARDING THE ASSETS OF A DECEASED MEMBER

We have also changed how we deal with the account of a member who dies. When we're notified about the death we will now switch the deceased member's account into cash or an alternative cash-based fund, as this will protect the value of the assets against market fluctuations.

YOUR FEEDBACK

We hope that you approve of these changes and we would be very interested to hear what you think about these new developments or any other aspect of our service.

Fidelity DC Client Management Team

Alan Salamon
Head of DC Client Management
01737 837528

David Alchin
Relationship Director
01737 836478

Tony Dibben
Relationship Director
01737 836877

Georgie Edwards
Relationship Director
01737 837592

Andrew Hughes
Relationship Director
01737 837691

Janet McMorrow
Relationship Director
01737 837289

Martin Speakes
Relationship Director
01737 837167

Andrew Worby
Relationship Director
01737 836354

Samantha Dixon
Senior Manager, Business Team
01737 836355

Richard Brewerton
Associate, Business Team
01737 837166

Lana East
Associate, Business Team
01737 834426

Rita Galbraith
Assistant Manager, Business Team
01737 837622

BILL'S DILEMMA