

Heritage With Profits Fund Investment Report: UK Pension Business

Q3 2019

This leaflet gives information on the following

- factors that affect with-profits plan values
- types of assets – how these affect investment returns
- investment market conditions
- asset mixes – the asset mix for different classes of with-profits pension business
- asset and investment return details for each asset mix



This leaflet is intended for individuals who are familiar with investment terminology. If you need an explanation of the terms used email us at wpreport@standardlife.com. Please note that there is no guarantee that any email sent will be received, or that the contents will remain private during internet transmission.

Factors that affect with-profits plan values

The return on the asset mix is only one of the factors that affect with-profits plan values. Other factors are the deductions we make, and any other discretionary adjustments that we may apply such as smoothing. The deductions are for example for costs of guarantees and our expenses.

When Standard Life demutualised on 10 July 2006 the Heritage With-Profits Fund was set up with an Inherited Estate. At least once a year we review whether it's appropriate to make distributions from the Inherited Estate. We use any distributions that we make to enhance with-profits payouts.

The value of with-profits investments can go down as well as up. Some with-profits plans guarantee a minimum payout, for example if it's used to buy an annuity at the retirement date selected at the start of the plan or on death. The payout will then be at least the guaranteed benefit, even if the investment returns have been poor.

For more information on with-profits please see our With-Profits guides available on our website at www.standardlife.co.uk/withprofitsguides

Types of assets

We invest in a wide range of assets including equities, property, bonds and cash deposits. We expect that a higher proportion of equities and property will produce returns that are higher over the long term, but more variable over the short term. We expect that a higher proportion of bonds and cash will result in returns that are more stable, but lower over the long term.

Investment Market Conditions

- Global equities finished in positive territory
- The US-China trade war rumbled on
- The US Federal Reserve cut interest rates twice
- Government bonds up for the quarter
- UK commercial real estate weakened further

UK Equities

Despite facing numerous challenges, UK stocks were up for the July-September period. The quarter started well as sterling weakness boosted companies that make a significant proportion of their profits overseas. Thereafter, markets worsened. The gilt yield curve inverted – a leading indicator of recession. Meanwhile, Boris Johnson became UK prime minister, increasing the chances of a no-deal Brexit. However, equities rallied in September as the US-China trade dispute took a more hopeful turn. News the UK parliament had passed legislation to prevent a no-deal scenario was also positive. Economic news was disappointing, with the UK economy contracting by a higher-than-expected 0.2% in the second quarter.

Overseas Equities

It was a positive three months for US equities, although trade tensions with China continued to ebb and flow. In August, President Trump announced fresh tariffs on \$300 billion of Chinese goods. China hit back with new taxes of 5-10% on \$75 billion worth of US products. A more conciliatory tone prevailed in September and both sides made concessions. They also agreed to resume talks. Meanwhile, the Fed cut rates on two occasions, citing concerns about global economic growth. In Washington, the Democratic Party opened formal impeachment proceedings against Donald Trump.

Europe's equity markets gained over the review period. This was primarily due to the ECB's decision to cut interest rates and restart its bond-buying programme. The reason behind the moves is less positive. Germany is teetering on the brink of recession. Growth in Europe's largest economy slowed by 0.1% in the second quarter compared to the previous three months.

Japanese stocks made strong gains, thanks to optimism about trade deals and potential interest rate cuts. However, risk aversion took hold in August as the US-China relationship deteriorated. That said, corporate results were a bright spot. Meanwhile, Prime Minister Abe's election success freed him to increase the consumption tax on 1 October. For many, this is a risky move for an economy feeling the effects of the global slowdown.

Asian markets were down for the period, as the US-China trade dispute took its toll. The mood initially soured as each side announced further tariffs. The supporting rhetoric also hardened and markets tumbled.

Fixed Interest

Global government bond indices posted gains over the quarter. In August, prices in the 'core' markets of the US, Germany and the UK moved sharply higher. This was in reaction to a clutch of concerns. Chief among them was the threat of global recession and anxiety over the escalation of the US-China trade dispute. Politics also played a part, including turmoil in Italy and the ongoing Brexit saga in the UK. During September, US Treasuries reversed direction, delivering their worst monthly performance in a year. The catalyst was a reassessment by the Fed of its outlook for interest rates. While there was a 0.25 percentage point cut mid-month, in the accompanying statement the Fed said it anticipated no further rate cuts in 2019.

Global corporate bonds continued to rally in the third quarter, driven by a sharp reduction in US Treasury yields (prices rose). In particular, the 10-year yield fell by a further 0.33% to 1.67%. This was a substantial 1.4% lower than a year earlier and reflected growing economic concerns. As a result, corporate bonds were seen as a more attractive investment than Treasuries. It was a similar story in Europe, where increasingly negative German bund yields were the main positive driver of European corporate bond returns.

Property

Total returns at an 'all property' level remained positive, but UK commercial real estate weakened further this quarter. While a summer lull is not abnormal, transaction volumes were particularly low this year. The weaker deal flow continued into September. Prolonged macroeconomic and political uncertainty is stifling market activity and affecting investor sentiment. A wide spread of returns at the sector level persists, with retail in negative territory and industrials significantly outperforming – especially in the South East.

Asset Mix

Our aim when managing our with-profits business is to provide growth over the long term, while continuing to maintain an appropriate level of financial strength so that we can meet all contractual obligations to our customers. We currently have five different asset mixes that cover most of our pensions business.



For information on Stakeholder plans taken out from 10 July 2006 onwards, please see the investment Report for the UK Smoothed Managed With-Profits Fund

Class of with-profits business	Fund Name (see your plan statement)	Asset Mix	Page
Unitised pensions for which a minimum unit price growth rate of 4% a year applies	Pension With-Profits Fund	Asset Mix 1	3
Most other unitised pensions	Pension With-Profits One Fund Pension 2 With-Profits 2 Fund Pension Millennium With-Profits Fund Pension With-Profits One 2006 Fund Pension 2 With-Profits 2 2006 Fund Pension Millennium With-Profits 2006 Fund	Asset Mix 3	4
With-Profits Pension Annuities	N/A	Asset Mix 4	5
Non unitised pensions	N/A	Asset Mix 5	6
Stakeholder plans taken out before 10 July 2006	Stakeholder With-Profits Fund Corporate Stakeholder With-Profits Fund	Stakeholder	7

We regularly review the asset mix that backs our with-profits business, taking account of such things as:

- the nature and size of the guarantees for each class of with-profits business
- the strength of the fund
- any changes in current and expected future market conditions.

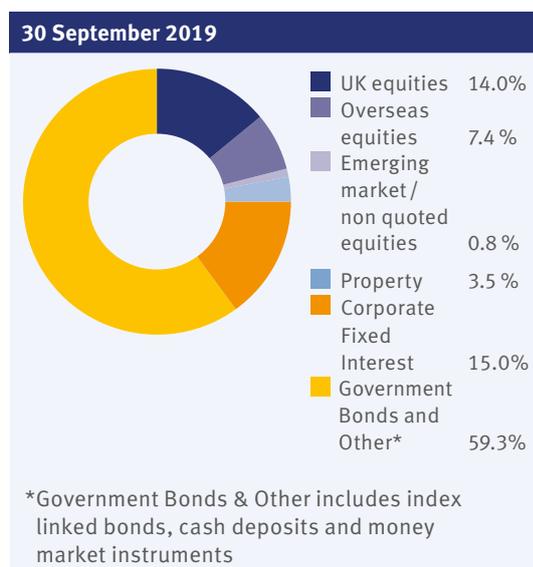
Note: the asset mix will also change as market values change.

Any change in the asset mix is likely to result in a change in future returns and plan payouts, see page 1 – Types of assets and Factors that affect with-profits plan values. But it will not affect existing guarantees.



For information on our guaranteed growth and regular bonus rates, please see our Pensions bonus rates leaflet. You can get a copy at www.standardlife.co.uk/withprofitsguides

Asset Mix 1: With-Profits Fund



Top 5 Equity Holdings

1. BP
2. Glaxo Smith Kline
3. HSBC
4. Astra Zeneca
5. British American Tobacco

Top 5 Bond Holdings

1. UK Govt 4.25% 2040
2. UK Govt 3.5% 2068
3. UK Govt 4.25% 2055
4. UK Govt 4.25% 2032
5. UK Govt 4% 2060

Corporate Bond portfolio

- 99% rated investment grade bonds of which
- 11% AAA rated as measured by a composite rating structure, derived from Standard & Poor's and Moody's ratings.



These investment returns do not allow for charges, expenses or the effects of any smoothing and have been rounded down.

Customers should refer to their annual statements to see how the value of their plan changes over time.

These figures refer to the past. Past Performance is not a reliable guide to future performance.

Investment returns: Last four quarter years

Quarter year ending on:	31/12/18	31/03/19	30/06/19	30/09/19
Asset Mix 1	-1.7%	3.4%	1.7%	2.6%

Asset Mix 1 is predominately invested in fixed interest and other bonds, in particular government bonds. This reflects the relatively higher guarantees provided by the classes of business backed by Asset Mix 1. The returns in Q3 reflect the positive returns in most asset classes tempered to an extent by a fall in property.

Asset mix details for last five calendar years

Asset mix as at 31 December	2014	2015	2016	2017	2018
UK Equities	10%	8%	8%	10%	11%
Overseas Equities	5%	4%	3%	6%	6%
Emerging Market / non quoted equities	3%	2%	3%	1%	1%
Property	5%	6%	5%	4%	4%
Fixed Interest & Other*	77%	80%	81%	79%	78%

*Fixed Interest & Other includes Corporate fixed interest, Government bonds including index linked bonds, cash deposits and money market instruments.

Investment returns: last five calendar years

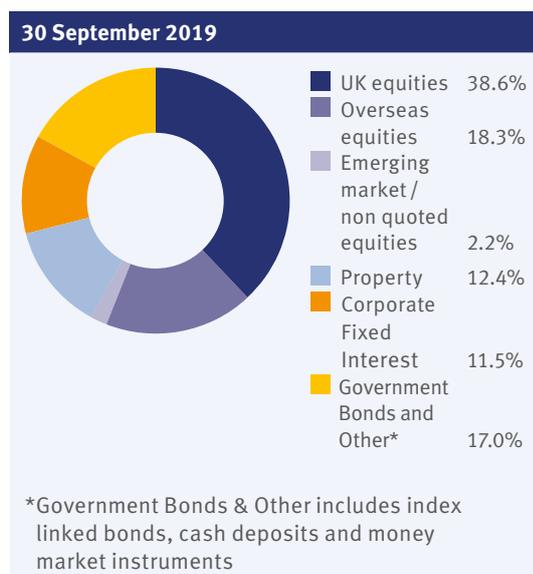
2014	2015	2016	2017	2018
9.9%	1.7%	8.8%	3.4%	-1.6%

For more information on with-profits please see our With-Profits guides available on our website at www.standardlife.co.uk/withprofitsguides



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Asset Mix 3 - See Page 2 for list of funds applicable



Top 5 Equity Holdings

1. BP
2. Glaxo Smith Kline
3. HSBC
4. Astra Zeneca
5. British American Tobacco

Top 5 Bond Holdings

1. UK Govt 4% 2022
2. UK Govt 2.25% 2023
3. UK Govt 0.75% 2023
4. UK Govt 1% 2024
5. UK Govt 1.5% 2021

Corporate Bond portfolio

- 99% rated investment grade bonds of which
- 11% AAA rated as measured by a composite rating structure, derived from Standard & Poor's and Moody's ratings.



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Investment returns: Last four quarter years

Quarter year ending on:	31/12/18	31/03/19	30/06/19	30/09/19
Asset Mix 3	-7.1%	5.7%	2.0%	2.1%

Asset Mix 3 is predominately invested in equities, in particular UK equities. The returns in Q3 reflect the positive returns in most asset classes tempered to an extent by a fall in property.

Asset Mix details for last five calendar years

Asset mix as at 31 December	2014	2015	2016	2017	2018
UK Equities	32%	31%	32%	35%	36%
Overseas Equities	15%	14%	14%	16%	16%
Emerging Market / non quoted equities	3%	3%	2%	2%	2%
Property	16%	16%	15%	13%	13%
Fixed Interest & Other*	34%	36%	37%	34%	33%

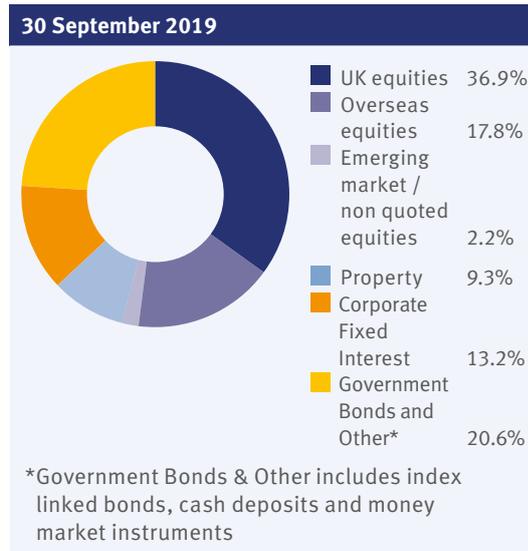
*Fixed Interest & Other includes Corporate fixed interest, Government bonds including index linked bonds, cash deposits and money market instruments.

Investment returns: last five calendar years

2014	2015	2016	2017	2018
8.3%	3.2%	12.2%	7.9%	-5.1%

For more information on with-profits please see our With-Profits guides available on our website at www.standardlife.co.uk/withprofitsguides

Asset Mix 4: With-Profits Pension Annuities



Top 5 Equity Holdings

1. BP
2. Glaxo Smith Kline
3. HSBC
4. Astra Zeneca
5. British American Tobacco

Top 5 Bond Holdings

1. UK Govt 4% 2022
2. UK Govt 2.25% 2023
3. UK Govt 0.75% 2023
4. UK Govt 1.5% 2021
5. UK Govt 1.75% 2022

Corporate Bond portfolio

- 99% rated investment grade bonds of which
- 11% AAA rated as measured by a composite rating structure, derived from Standard & Poor's and Moody's ratings.



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Customers should refer to their annual statements to see how the value of their plan changes over time.

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Investment returns: Last four quarter years

Quarter year ending on:	31/12/18	31/03/19	30/06/19	30/09/19
Asset Mix 4	-6.7%	5.8%	2.1%	2.5%

Asset Mix 4 is predominately invested in equities, in particular UK equities. The returns in Q3 reflect the positive returns in most asset classes tempered to an extent by a fall in property.

Asset mix details for last five calendar years

Asset mix at 31 December	2014	2015	2016	2017	2018
UK Equities	30%	29%	30%	31%	34%
Overseas Equities	13%	13%	13%	15%	16%
Emerging Market / non quoted equities	3%	2%	2%	2%	2%
Property	14%	14%	13%	13%	10%
Fixed Interest & Other*	40%	42%	42%	39%	38%

*Fixed Interest & Other includes Corporate fixed interest, Government bonds including index linked bonds, cash deposits and money market instruments.

Investment returns: last five calendar years

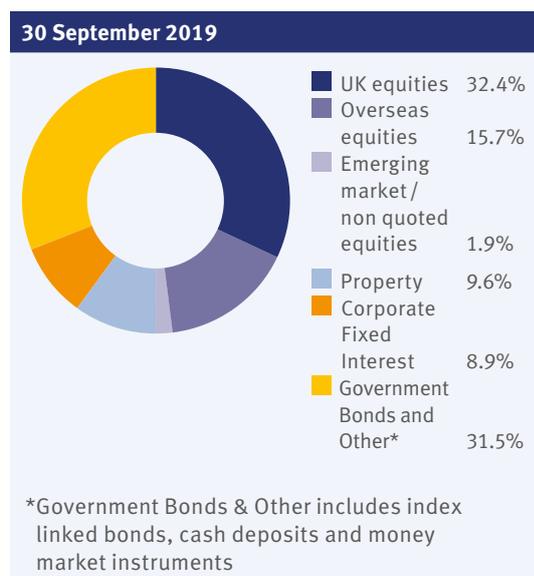
2014	2015	2016	2017	2018
8.9%	2.9%	12.4%	7.6%	-5.0%

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Asset Mix 5: Non utilised pensions



Top 5 Equity Holdings

1. BP
2. Glaxo Smith Kline
3. HSBC
4. Astra Zeneca
5. British American Tobacco

Top 5 Bond Holdings

1. UK Govt 2.25% 2023
2. UK Govt 4% 2022
3. UK Govt 0.75% 2023
4. UK Govt 1% 2024
5. UK Govt 1.5% 2021

Corporate Bond portfolio

- 99% rated investment grade bonds of which
- 11% AAA rated as measured by a composite rating structure, derived from Standard & Poor's and Moody's ratings.



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Investment returns: Last four quarter years

Quarter year ending on:	31/12/18	31/03/19	30/06/19	30/09/19
Asset Mix 5	-5.8%	4.9%	1.8%	2.0%

Asset Mix 5 is predominately invested in government bonds and UK equities. The returns in Q3 reflect the positive returns in most asset classes tempered to an extent by a fall in property.

Asset mix details for last five calendar years

Asset mix at 31 December	2014	2015	2016	2017	2018
UK Equities	20%	16%	21%	27%	29%
Overseas Equities	10%	9%	9%	14%	14%
Emerging Market / non quoted equities	3%	4%	2%	2%	2%
Property	19%	21%	19%	12%	10%
Fixed Interest & Other*	48%	50%	49%	45%	45%

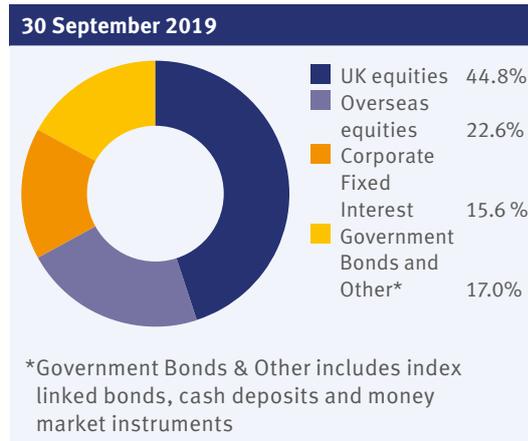
*Fixed Interest & Other includes Corporate fixed interest, Government bonds including index linked bonds, cash deposits and money market instruments.

Investment returns: last five calendar years

2014	2015	2016	2017	2018
6.5%	2.9%	8.2%	6.1%	-4.1%

For more information on with-profits please see our With-Profits guides available on our website at www.standardlife.co.uk/withprofitsguides

Stakeholder Asset Mix Details



Top 5 Equity Holdings

1. Glaxo Smith Kline
2. BP
3. HSBC
4. Astra Zeneca
5. British American Tobacco

Top 5 Bond Holdings

1. UK Govt 4.25% 2040
2. UK Govt 3.5% 2068
3. UK Govt 4.25% 2055
4. UK Govt 4.25% 2032
5. UK Govt 4% 2060

Corporate Bond portfolio

- 99% rated investment grade bonds of which
- 7% AAA rated as measured by a composite rating structure, derived from Standard & Poor's and Moody's ratings.



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Investment returns: Last four quarter years

Quarter year ending on:	31/12/18	31/03/19	30/06/19	30/09/19
Stakeholder With-Profits Fund and Corporate Stakeholder With-Profits Fund	-9.4%	7.6%	2.7%	3.1%

The Asset Mix for the Stakeholder Funds is predominately invested in equities, in particular UK equities. The returns in Q3 reflect the positive returns in all asset classes.

Asset mix details for last five calendar years

Asset mix at 31 December	2014	2015	2016	2017	2018
UK Equities	42%	42%	44%	47%	45%
Overseas Equities	23%	20%	21%	22%	22%
Fixed Interest & Other*	35%	38%	35%	31%	33%

*Fixed Interest & Other includes Corporate fixed interest, Government bonds including index linked bonds, cash deposits and money market instruments.

Investment returns: last five calendar years

2014	2015	2016	2017	2018
6.6%	0.8%	16.6%	9.9%	-7.9%

For more information on with-profits please see our With-Profits guides available on our website at www.standardlife.co.uk/withprofitsguides

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