Smart Pension Master Trust Investment Report Quarter 3 2021

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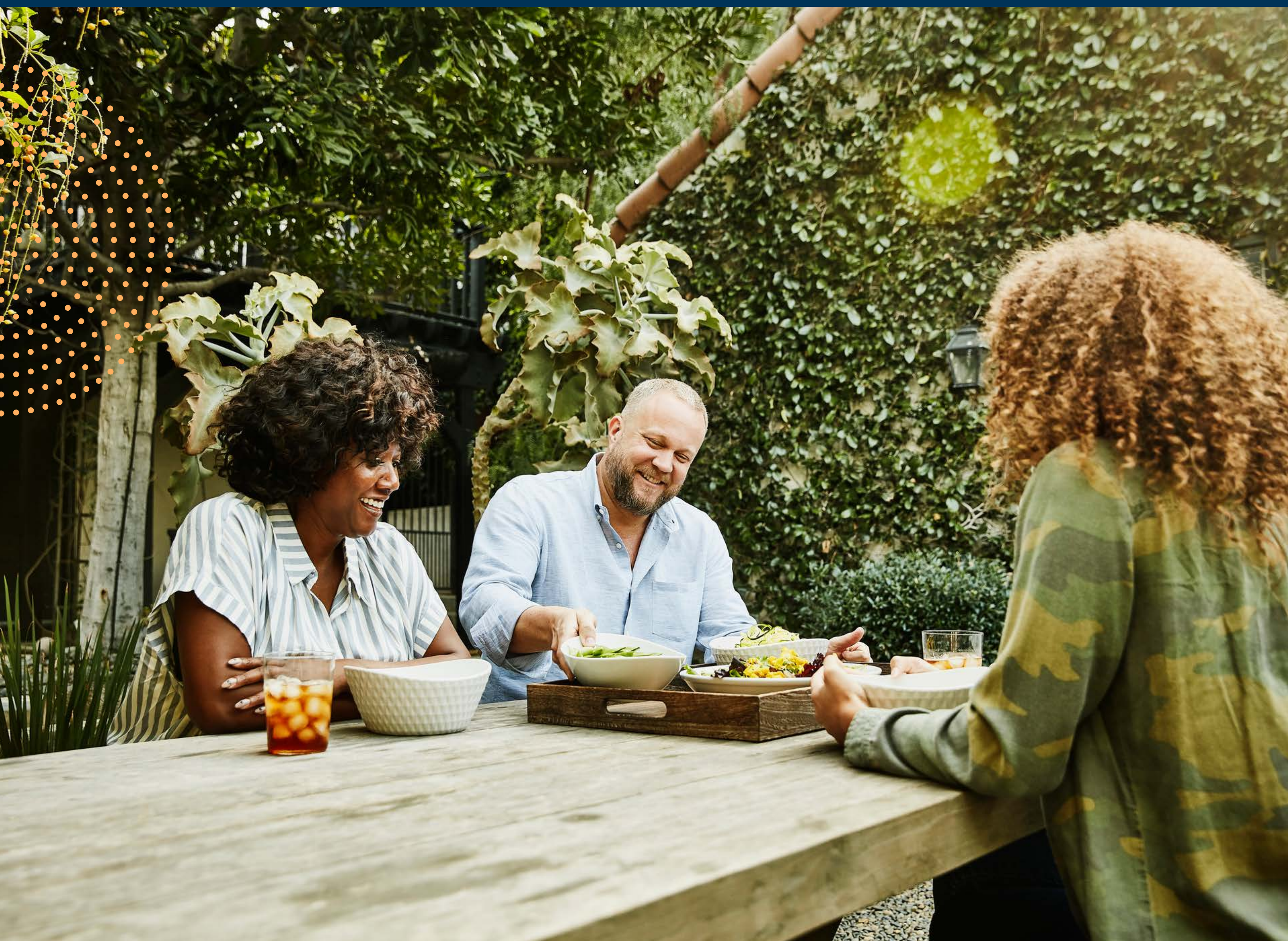
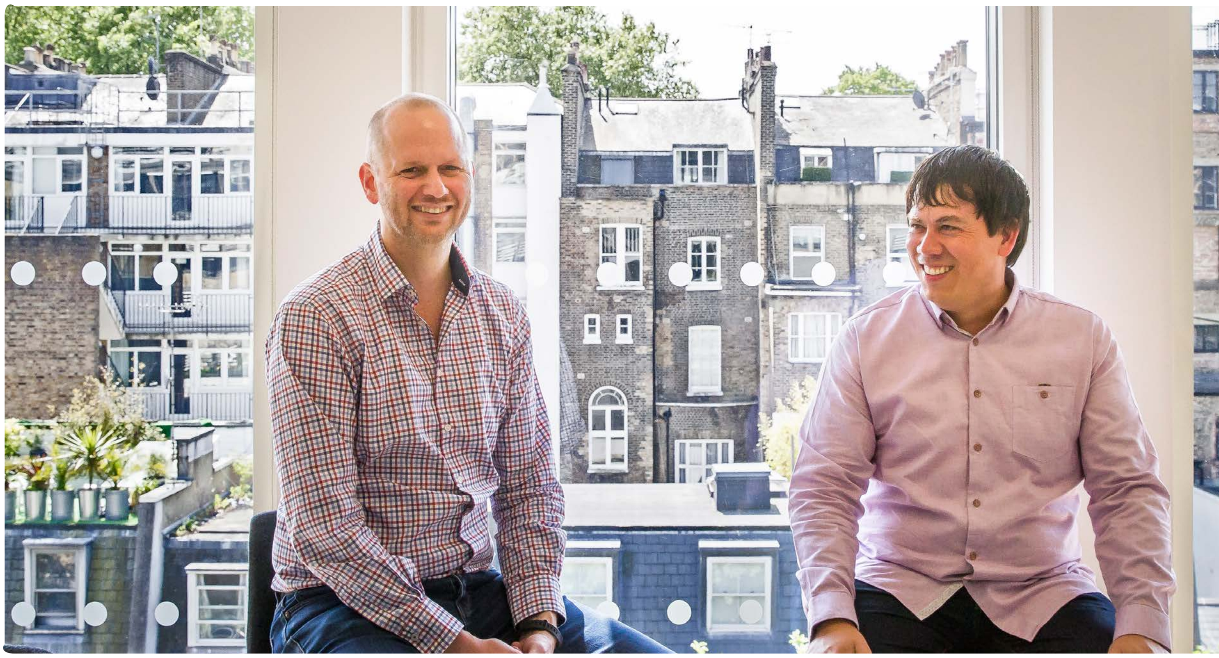


Welcome to your investment report

This report is for all members of the Smart Pension Master Trust. As a member, your money is invested in one, or a combination, of our funds. If you do not make an active choice, your money is invested in our default strategy. This is designed by the trustee of the scheme to be suitable for most members and it solely uses our default fund, Smart Growth – Moderate Risk, up to eight years prior to your chosen retirement date, when additional funds (Smart Income, Smart Annuity and Smart Cash) are also used.



Will Wynne, Group Managing Director and Group Andrew Evans, CEO

Pensions are an investment. As a pension saver, your savings will be affected by a whole host of factors that influence the returns of, for example, stocks and shares over the lifetime of your savings. The first section of this report outlines what has generally been happening in financial markets and the economy over the last three months, and why you may have seen your pension savings grow or shrink.

Remember, markets can go up and down quite a lot over the short term. Pensions are a long-term investment and, as our funds are invested for the long term, this report should not be used to make investment decisions. It also gives a generalised view and is not specifically focused on any single fund.

Our investment strategies are made up of multiple different funds that react differently to market events.

That's why, in the second section of this report, we have included the most recent performance data for all our funds. This shows you how they have been performing over the past three months, six months, one year, three years and five years. How your own savings are doing will relate to these performance figures.

We have included a glossary at the end to help you with any jargon that may be unfamiliar to you.

Contents

What's been happening in the markets?

The default fund: performance overview

The default growth phase fund continued to gain during the period July to September 2021. The widespread opening-up of economies across Europe and North America during the summer months continued to drive positivity in financial markets higher for most of the period, although there was some widespread weakness in September.

The Smart Growth – Moderate Risk fund gained 2.5% in the three months to September, bringing performance in 2021 to +11.6%. The fund continues to outperform the targets for long-term pension savings over one, three and five years, to the benefit of future retirement income.

As has been the case since the market recovery began at the end of 2020, equities were the strongest performers and the major contributor to the performance of the growth phase of the default fund for the quarter. Fixed income markets also contributed to the overall performance, albeit to a lesser extent. However, both equities and bonds fell during September, reducing overall gains.

The big events

Economic recovery supported by vaccine rollouts, but growing concerns

Equity markets mildly supported during the quarter

Fixed income markets starting to price in future rate rise

High inflation, led by energy prices

Further gains but growing concerns

Market conditions in the first two months of the third quarter were much the same as those in the second quarter. Financial markets continued to perform well almost across the board, with many equity markets continuing to hit new highs. However, September proved to be a significant speed bump, as growth and inflation concerns became more prominent and a surge in natural gas prices became a major problem in many countries, including the UK.

For much of 2021, conditions have been positive for financial markets, equities in particular. Investors are typically forward-looking and the focus has been on the economic recovery. Vaccine rollouts gathered pace in many countries and supported strong earnings growth. Equally important has been the huge amount of stimulus, both fiscal and monetary. Fiscal stimulus (or government spending) prevented a sharp collapse of economies and gave confidence to financial markets. Monetary stimulus in the form of ultra-low interest rates has been a significant driver of asset prices, along with bond-buying by central banks. When interest rates are low, investors seek riskier assets with higher returns, such as equities, commodities and property.

A major concern through the year has been rising inflation, primarily a result of supply shortages across economies due to a sharp demand recovery and continued disruptions to production. When inflation expectations increase, longer-term interest rates rise (in the form of bond yields) and make risky assets less attractive. Whereas earlier in the year there was confidence that the spike was temporary, by September forecasts were being changed significantly. Supply shortages had also been seen as a temporary headwind, but their negative impact has started to become more problematic, with significant production outages being felt across many sectors. These shortages have extended to the labour market, most visibly in the UK where a shortage of HGV drivers led to a fuel supply crisis. However, this labour shortage is being experienced in many countries, particularly in Europe, as certain sectors have found it difficult to attract new entrants for some time.

The extent to which recent market weakness continues will be dependent on how persistent all these issues continue to be. Inflation and supply shortages have been in the background throughout the year and are largely related. If vaccine rollouts and slowing infections reduce the number of shutdowns and disruptions, these shortages should start to ease over time. Higher energy prices look set to stay for some time, though, given the time lags involved in increasing production.

How have global equities performed?

Developed market equities ended the third quarter with small gains in local currency terms as positive performance in July and August was reversed in September. Momentum remained strong in July and August, supported by the ongoing economic recovery and strong corporate earnings against a backdrop of loose monetary policy. The reversal in September was triggered by renewed concerns about inflation and downgrades of economic growth expectations. However, emerging markets fell sharply.

US equities showed a small positive return during the period. Major stock market indices continued to make new highs up to early September, led by strong earnings from technology companies. However, the continued rise in inflation at a relatively early stage in the recovery has led to concerns of faster than expected tightening of monetary policy. The Federal Reserve has now indicated that it will begin to withdraw monetary stimulus before the end of 2021 whilst raising inflation forecasts from 3.4% to 4.2%. At the same time, growth downgrades have led to concerns that the recovery is slowing. On a specific sector basis, financials did well as rising interest rates help their margins. Additionally, the energy sector performed strongly in September due to rising natural gas and oil prices.

UK equities rose during the third quarter and were more resilient in September. This was driven in part by a wave of takeover bids, as the UK market is seen as attractive for overseas acquirers and private equity investors seeking to take companies off public markets. Supermarket chain Wm Morrison was subject to rival bids and drove the whole sector higher. There were also takeover offers in the industrials and gaming sectors. UK equities were further helped by the composition of the market, where oil and gas companies and financials have a larger weighting and were supported by the rising oil price and higher bond yields respectively. Previously the UK market had lagged due to being made up of fewer technology stocks.

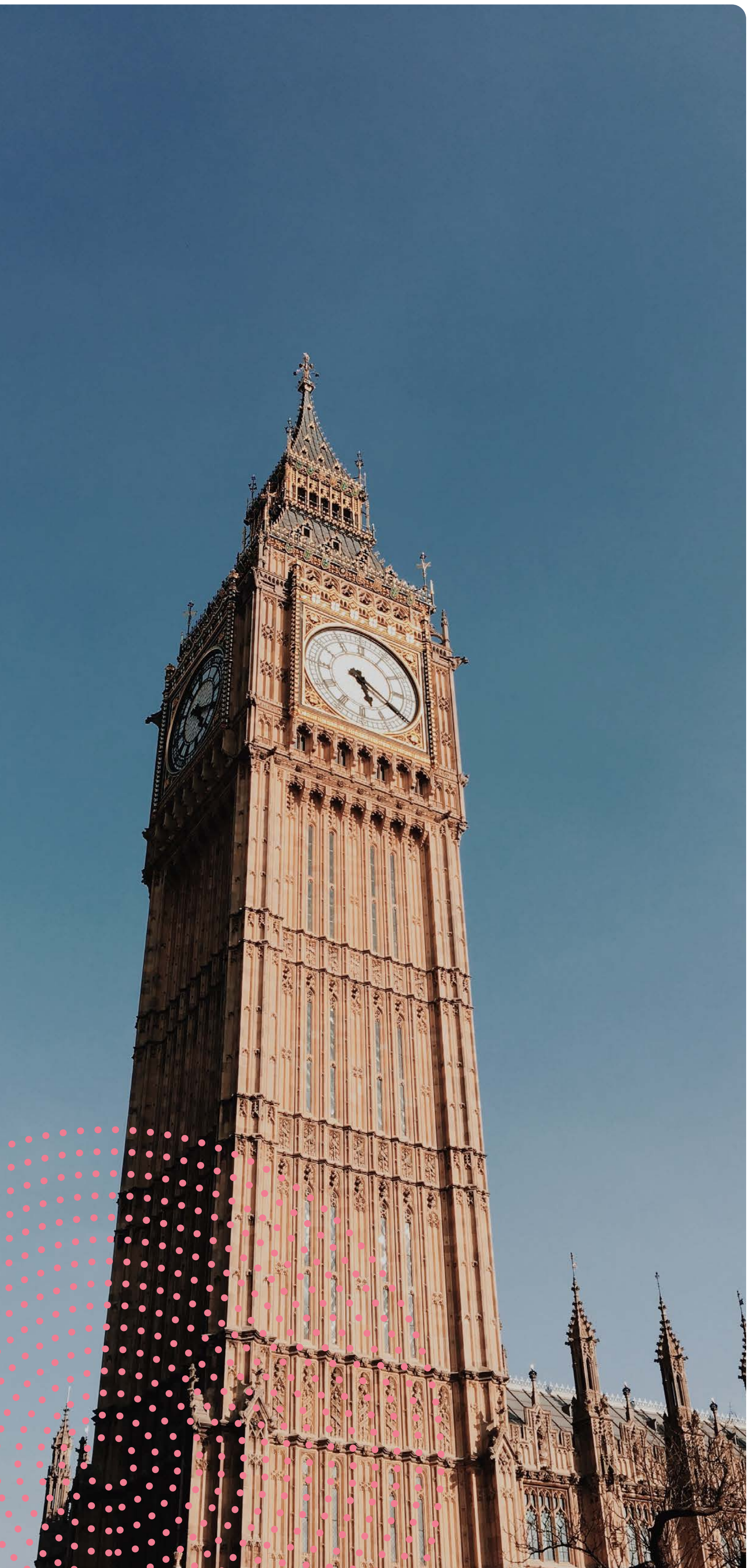
Japan was the best-performing developed market and rose during September. Sentiment was helped by a surprise change of Prime Minister. In addition, Japan's vaccine rollout accelerated after the country had been hit by rising infections early in the summer. In contrast, European markets were flat. Industrial production is coming under pressure from supply chain shortages. This is particularly the case in Germany, where car production is a big sector of the economy. The surge in energy prices and higher inflation were headwinds across the region.

Emerging markets as a whole were a significant underperformer throughout the quarter as they faced multiple negative factors. Developments in China in particular have put pressure on the stockmarket. Potentially the most serious of these are the troubles in the property sector. China Evergrande, the largest developer, is on the verge of collapse as it is unable to make interest payments on its huge $300 billion of debt.

The property sector has been a major driver of economic growth for many years. If problems spread across the sector, they could prove to be a significant problem for the Chinese economy. At the start of the quarter technology and education stocks were also sold off heavily as the government launched a regulatory crackdown.

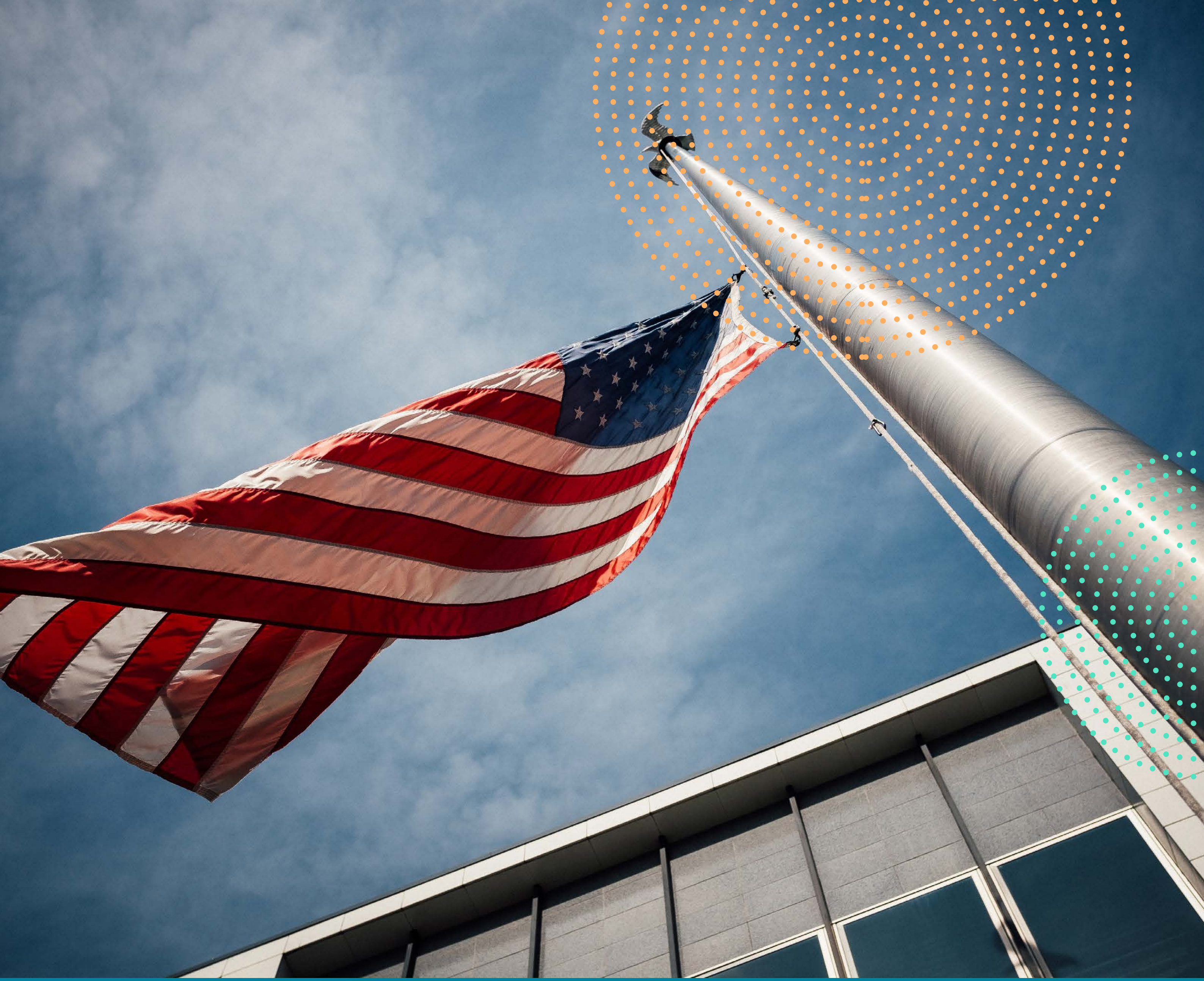
A look at government and corporate bonds

Overall, fixed income markets were able to deliver mild positive returns during the quarter but ran out of momentum towards the end of September. Government bonds are usually seen as having low volatility, meaning their prices do not move as much as those of, for example, equities. As a result of this greater predictability, investors are willing to accept lower returns in order to hold them. However, during the course of 2021 this hasn't been the case. Government bonds have become more volatile and have delivered flat or negative returns.



The reason for the rise in bond yields (and lower bond prices) since mid-September has been the resurfacing of concerns about the inflation outlook. Financial markets and central banks had mostly been less worried about inflation in the belief that it will be short-lived. If long-term inflation expectations rise, investors require higher interest rates in order to hold bonds, which in turn means bond prices fall. The continued rise in energy prices has raised concerns that inflation may be more persistent and will start to pass through into other goods and services, leading to a more inflationary cycle.

Adding to this concern has been the expansion of supply shortages seen across different parts of the economy. Much attention in the UK has focused on the shortage of HGV drivers to deliver petrol and consumer products. Yet this is a shortage seen across the whole of Europe, as the industry has failed to attract sufficient new entrants for several years. This is being seen in other sectors of the economy and, as a result, supply chain shortage is an ongoing impact from the pandemic. Higher wages also lead to higher longer-term inflation expectations, but this is not necessarily negative for the overall health of the economy. However, interest rates and bond yields began the year at record low levels, which is why a higher inflation outlook has such a big impact.



US and European government bonds were generally flat during the quarter. UK government bonds fell, with the yield on ten-year bonds rising from 0.72% to 1.02% as the Bank of England suggested short-term rates may rise sooner than expected from the current 0.1% if inflation remained high. Corporate bonds changed little, following the pattern of most government bonds. Emerging market bonds were weak, though, as many currencies fell sharply against the US Dollar and concerns about the property sector in China hurt sentiment across the whole sector.

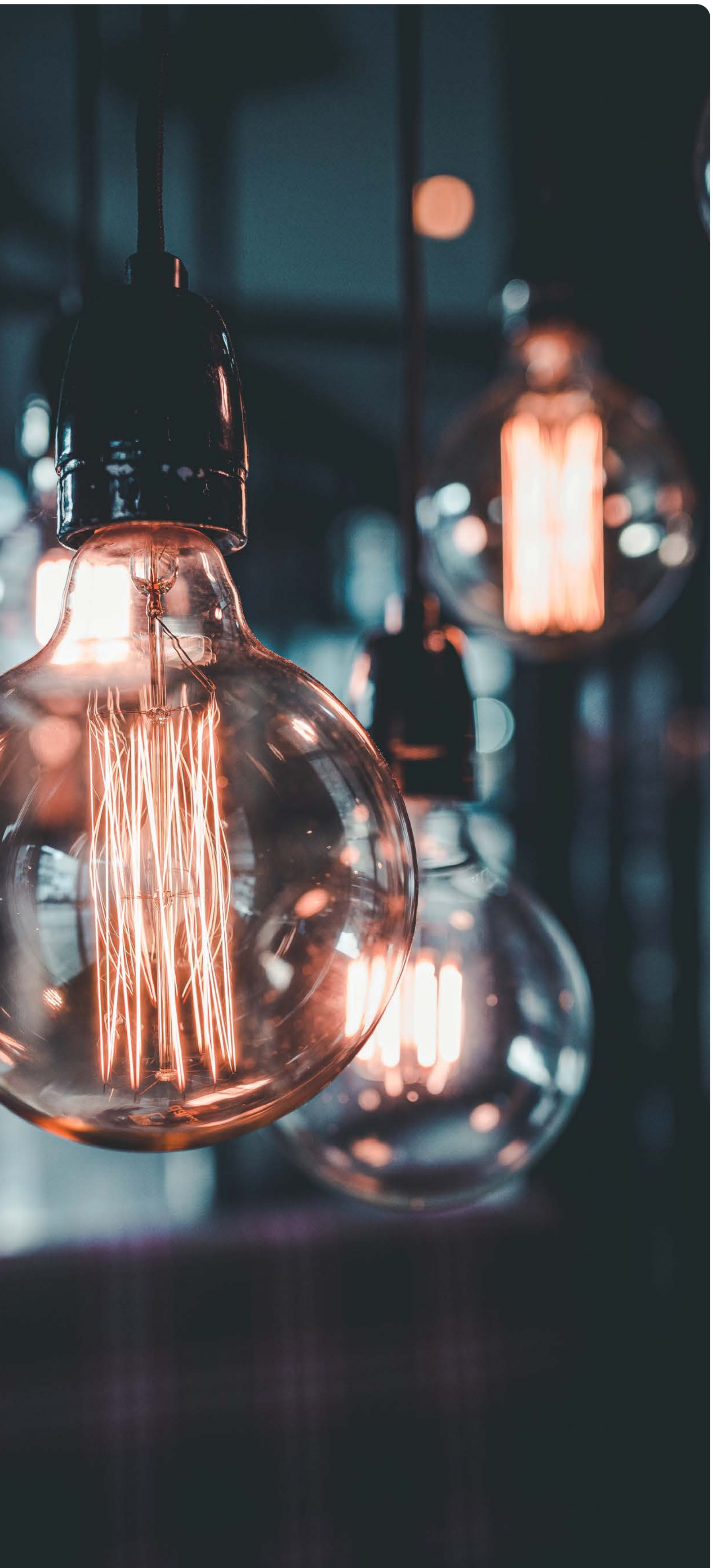
A strong US Dollar

The main currency mover in the period was the US Dollar, which rose against all major currencies, continuing the strong performance seen for much of the year. A primary reason for its relative strength is the expectation that the Federal Reserve will be amongst the first central banks to begin tightening monetary policy by ending its bond purchase programme, also known as quantitative easing. This is partly due to the US experiencing a faster recovery and higher inflation rate than Europe and other countries. More recently, it reflects concerns over slowing global growth as supply chain shortages continue to impact upon recovery. The US Dollar often does well during such periods because it is often seen as a safe haven currency.

The British Pound fell against the Dollar, with one Pound buying less than 1.35 Dollars at the end of the quarter, down from a rate of 1.42 earlier in the year. However, despite the well-documented shortages in the UK economy, the Pound hardly changed against the Euro, reflecting the fact that Dollar strength was the main market driver. In contrast, emerging market currencies were weak, reflecting slower growth and, in many cases, the ongoing slow speed of vaccine rollout.

Commodities: Soaring energy prices

The positive performance of commodities continued in the thee months to September and this remains the best-performing asset class in 2021. The S&P GSCI Index, a basket of commodities, is now up 38.2% for the year. However, performance has been mixed within the different commodities. Whilst energy prices continued to accelerate, the prices of many metals have started to come under pressure and have been falling recently.



The most visible movement has been in natural gas prices, a result of both short-term and longer-term factors. Much of Europe and North Asia experienced a colder and more prolonged winter in the first half of the year, which reduced levels of gas storage. As economic activity picked up, there was a surge in demand for natural gas. At the same time, supply has been constrained from many suppliers, partly as a result of price weakness in 2020 curtailing investment. The price rise has been global, although the UK has been the worst-affected as it has limited storage capacity and is therefore more dependent on imports.

At the end of September, wholesale gas prices were up more than 400% on the year and continued accelerating after the end of the quarter. Similar increases have been seen in Europe and even in the US (despite being self-sufficient in gas) where prices have risen 130% during the year. Although recent increases are excessive and could pull back, gas prices could remain elevated for some time as we head into the colder months due to demand rise and low inventory levels, especially in case of a cold northern hemisphere winter.

Away from the energy sector, the period saw a decline in many other commodity prices. Iron ore, used in steel production, fell more than 50%, and other metals were also weak as measures in China to limit speculation and weakness in the property sector hurt demand. However, it is worth noting that the European carbon price, which puts a cost on harmful emissions, continues to rise and is up almost 90% during the year. This is important because it supports the transition to more environmentally-friendly industrial production processes.

How have our funds performed?

This quarter's performance tables

These tables show you the returns for each of our funds over different time periods. All values are as of 30 September 2021.

All values are shown before Annual Management Charges (AMCs) are deducted. You can learn more about the charges applicable to you from your tailored investment guide within the secure section of your account.

The performance tables show both annualised and cumulative returns.

The cumulative return (CR) is the total return on your investment over that period. The annualised return (AR) is the equivalent annual return you would have received for each year in the period.

For example, a 30% cumulative return over three years is equivalent to a 9.1% annualised return.

Model strategies

Growth phase	3m	6m	1y	3y	5y
Smart Growth – Lower Risk					
Fund (returns beyond 1y are annualised)	2.9%	8.8%	17.8%	7.5%	7.6%
Fund (cumulative returns)	2.9%	8.8%	17.8%	24.2%	44.0%
Benchmark (UK CPI +3%) (figures beyond 1y are annualised)			6.1%	4.8%	5.1%
Smart Growth – Moderate Risk (used in our default strategy)					
Fund (returns beyond 1y are annualised)	2.5%	8.4%	20.3%	7.3%	8.6%
Fund (cumulative returns)	2.5%	8.4%	20.3%	23.6%	51.3%
Benchmark (UK CPI +3.5%) (figures beyond 1y are annualised)			6.6%	5.3%	5.6%
Smart Growth – Higher Risk					
Fund (returns beyond 1y are annualised)	3.1%	9.3%	23.1%	7.6%	8.9%
Fund (cumulative returns)	3.1%	9.3%	23.1%	24.5%	53.1%
Benchmark (UK CPI +5%) (figures beyond 1y are annualised)			8.1%	6.8%	7.2%

“De-risking” phase	3m	6m	1y	3y	5y
Smart De-risking					
Fund (returns beyond 1y are annualised)	1.9%	5.8%	12.1%	5.7%	5.7%
Fund (cumulative returns)	1.9%	5.8%	12.1%	18.0%	31.7%
Benchmark (UK CPI +2%) (figures beyond 1y are annualised)			5.0%	3.8%	4.1%
Smart Lower Risk					
Fund (returns beyond 1y are annualised)	0.4%	1.1%	1.3%	1.2%	0.9%
Fund (cumulative returns)	0.4%	1.1%	1.3%	3.6%	4.7%
Benchmark (UK CPI +1%) (figures beyond 1y are annualised)			4.0%	2.8%	3.1%
Smart Cash					
Fund (returns beyond 1y are annualised)	0.0%	0.0%	0.0%	0.4%	0.4%
Fund (cumulative returns)	0.0%	0.0%	0.0%	1.2%	1.8%
Benchmark 3-month LIBOR (figures beyond 1y are annualised)	0.08%				
Smart Income					
Fund (returns beyond 1y are annualised)	0.6%	4.2%	9.2%	6.3%	5.8%
Fund (cumulative returns)	0.6%	4.2%	9.2%	20.1%	32.6%
Target benchmark (BOE rate + 3.5%) (figures beyond 1y are annualised)			3.6%	4.0%	3.9%
Smart Annuity					
Fund (returns beyond 1y are annualised)	-1.5%	0.8%	-4.5%	5.2%	2.4%
Fund (cumulative returns)	-1.5%	0.8%	-4.5%	16.5%	12.6%

Self-select funds

Self-select funds	3m	6m	1y	3y (AR)	5y (AR)	3y (CR)	5y (CR)
Smart UK FTSE100 Equity Index Fund	2.5%	7.6%	25.7%	2.3%	4.9%	7.0%	27.1%
Smart World (ex UK) Developed Equity Index Fund	3.6%	11.2%	24.8%	13.2%	14.3%	45.1%	95.0%
Smart All Stocks Index Linked Gilt Fund	2.2%	6.9%	0.0%	6.4%	2.7%	20.4%	14.0%
Smart North America Equity Index Fund	4.5%	13.4%	26.8%	15.7%	16.6%	54.7%	115.2%
Smart Cash Fund	0.0%	0.0%	0.0%	0.4%	0.4%	1.2%	1.8%
Smart Overseas Bond Index Fund - GBP Hedged	0.2%	0.9%	-2.3%	3.7%	1.5%	11.5%	8.0%
Smart World Emerging Markets Equity Index Fund	-4.1%	0.4%	14.0%	8.3%	8.5%	27.1%	50.3%
Smart Income Fund	0.6%	4.2%	9.2%	6.3%	5.8%	20.1%	32.6%
Smart Annuity Fund	-1.5%	0.8%	-4.5%	5.2%	2.4%	16.5%	12.6%
Smart Diversified Fund	1.6%	6.1%	13.5%	7.4%	6.9%	23.9%	39.8%
Smart Sharia Fund	3.8%	13.8%	20.2%	18.6%	17.6%	67.0%	124.5%
Smart Ethical Index Fund	3.8%	11.5%	25.9%	13.3%	14.2%	45.4%	94.4%
Smart Future Fund	2.8%	8.9%	22.3%	7.8%	8.2%	25.1%	48.5%

(figures beyond 1y are annualised)

How do we manage your money?

Your pension scheme is managed by a group of independent and non-affiliated trustees. They look after your interests and work for you. Your relationship is with the trustees, not Smart Pension Limited.

They keep an eye on:

- the investment strategy
- how your investments are performing
- value for money
- member communications
- member engagement

The trustees look after your money to ensure it is invested in line with the statement of investment principles.

The statement of investment principles is a trustee document that outlines the way trustees will invest the scheme assets. This also includes the trustees' policy on responsible investment (also known as Environmental, Social and Governance (ESG) issues).

The trustees work alongside fund managers and the scheme's investment manager to ensure performance is in line with the agreed benchmarks. You can view the statement of investment principles **here**.

Trustees

Andy Cheseldine, Chair of the Board

Andy is renowned for his deep knowledge and wealth of expertise in the pensions industry. His inclusion in the Top 50 People in Pensions Awards in 2015 and the Top 25 most influential investment consultants in the last five years is a testament to his reputation.

Anna Eagles, Trustee Director

Anna is a pensions actuary by background and a Fellow of the Institute and Faculty of Actuaries, with 22 years' experience advising trustees and employers. Before joining Law Debenture, she was with Willis Towers Watson Ltd.

Anna Darnley, Trustee Director

Before joining the board, Anna was a trustee of the Accenture Retirement Savings Plan. As a digital strategy consultant, she specialises in the Internet of Things, and has also worked on artificial intelligence and blockchain projects. She brings this technological expertise to the board, along with her passion for great member communications and re-engaging scheme members.

David Brown, Trustee Director

David has 30 years' experience in the pension and investment industry in the UK and Internationally working as an operator and consultant. During this period David has worked for two of the Big Four consulting firms and more recently at Tesco, where he was the UK and ROI Pensions and Payroll Manager.

Nikesh Patel, Trustee Director

Nikesh joined the board in 2021. He has a wealth of experience in consulting trustees and employers on defined benefit (DB) and defined contribution (DC) pension schemes. In 2019, he was recognised as a Rising Star in Asset Management by Financial News for his work managing pension scheme assets directly as a fiduciary investment manager.

The trustees would love to hear from you

The trustees are keen to get as much feedback as possible about how they can improve the pension scheme. If you have a suggestion, please do not hesitate to contact them at trustees@smartpension.co.uk.

Want to find out more?

For up to date information about the performance of your investments, you can download the Smart Pension app or sign in to SmartPension.co.uk/sign-in.

You can also download the investment guide to find out more information about your investment strategy.

You can also contact us for any other information relating to your pension savings at member@smartpension.co.uk.

Glossary

Bonds

A bond represents a loan made by an investor to a borrower and is often referred to as a fixed income security. This is because fixed interest payments are made as part of the returns. They can be issued by a government to raise money for things like infrastructure projects, or by private or public companies.

Central banks

Central banks around the world set the base interest rates of a country. The setting of these rates is part of something called monetary policy. For instance, increasing interest rates makes it more expensive to borrow and more profitable to save. In theory, this means people would spend less and save more, taking money out of circulation from the economy and reducing inflation rates. Reducing the interest rates level would have the opposite effects. Too high, very low or negative inflation rates can be bad for the economy.

Equities

Shares in publicly-traded companies such as Apple, Facebook, BP or HSBC. They are grouped in major indices depending on the country in which they are traded. (for instance the FTSE in the UK, or the Dow Jones in the US).

Equity index

An index is a number that represents the value of a group of stocks and shares, often combined by country and/or type of companies. For instance, the UK FTSE 100 is an index that represents the value of the largest 100 companies in the UK. Similarly, the Dow Jones Index is representative of the 50 largest companies in the United States.

Inflation

Inflation is a measure of the rate at which the average price of a "basket" of goods and services in an economy increases over a period of time. As the cost of goods rises, a single unit of currency for example, £1) buys fewer and fewer goods and services. This loss of purchasing power has an impact upon the general cost of living. Excessive inflation makes goods and services too expensive to buy and is bad for the economy.

Interest rate

An interest rate is the amount to be paid over a given period and is given as a proportion of the amount lent, borrowed or saved. For example, if you saved £100 in an account with a 1% annual interest rate, then after one year you would be paid £1 in interest.

Investment strategy

Is a way of investing your money over time with the aim of growing your pension savings. As you get closer to your retirement age, we move your money into funds that are less likely to fall in value.

The default fund

Unless you actively choose otherwise you will automatically be invested in our default fund during the growth phase, up to eight years before your selected retirement age. Our default fund is the Smart Growth – Moderate Risk fund. It has been created so that it will typically suit most of our members.

The default strategy

If you do not make an active investment choice, your savings will be invested according to the default strategy. It uses our default fund during the growth phase, and then switches to funds designed to protect your savings as you approach retirement. The full details of the default strategy can be found in our investment guide.

Volatility

Volatility refers to the amount of risk or uncertainty due to the size of changes in value (of currencies or equities).

Legal disclaimer

The value of investments may go up or down due to fluctuations in currencies, financial markets and other risk factors. Default funds may not fulfil their objectives: performance is not guaranteed and future performance may not be in line with the past. This report has been created by Smart Pension and is valid at the date it is published. It has been created for general information only and does not constitute specific legal advice or opinion. You should not rely on any of the information contained within this report without seeking further advice from qualified investment advisers. The facts and data contained in this report shall not be copied, made available, reproduced, extracted or published within your business, for commercial purposes, or to the public or for any other purposes unless Smart Pension gives you consent.

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