A tailored approach to cashflow-driven investment.

July 2021

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Liability Aware CDI Funds

Closed to new members, a growing number of defined benefit (DB) schemes are paying out more each year to members than income from contributions and investments.

This threat of turning 'cashflow negative' means a change of focus. Schemes are increasingly adopting a cashflow-driven approach. This means selecting assets that provide a contractual income which, as far as possible, match the scheme's future cashflow requirements.

Predictable and stable cashflow for your pension scheme

Small-to-medium-sized pension schemes are likely to seek out a pooled solution (unlike larger schemes which, targeting self-sufficiency, are likely to adopt a segregated approach).

We've created our **Liability Aware CDI fund range** with these schemes in mind, creating a bespoke cashflow payment profile that fits your scheme's future cashflow requirements. after allowing for contributions and income from other assets such as private debt or real estate.

How do our Liability Aware CDI funds work?

- Our fund range consists of four 3-year 'buckets', allowing your pension scheme to tailor its holdings to meet its cashflow requirements. We also have a wider range of longer-dated credit and gilt-based (leveraged and unleveraged) profile funds.
- We aim to provide your scheme a relatively predictable series of cashflow from a series of maturity dated cashflow funds. Managed on a buy & maintain basis, your portfolio consists of nominal corporate bonds, with coupons and redemption proceeds paid out over time.
- The funds are mainly invested in nominal GBP corporate bonds, targeting an average credit quality of A. The funds can also hold gilts and derivatives (including credit default swaps) and overseas bonds if these become appropriate to manage the portfolio efficiently.

Why invest in Liability Aware CDI?

A CDI approach has the explicit goal of maintain the shape of your cashflow profile, compared with a simple buy & maintain credit fund (where cashflows may vary over time).

Our CDI funds give your scheme:

A predictable and stable cashflow profile.

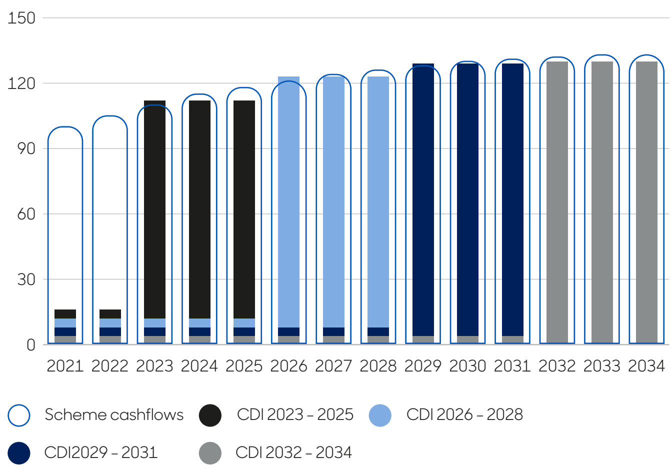
Rather than focusing on maximising returns, each fund aims for precision and certainty of cashflow delivery, giving your scheme a relatively stable pay-out profile per unit held.

Designed to suit your specific needs

We create a bespoke solution for your scheme by combining allocations across the fund range.

A strong track record of avoiding defaults and downgrades.

Our funds benefit from the experience of a credit team of more than 132 portfolio managers and analysts based across Europe, North America, Asia and Australia.



Source: abrdn.

Why abrdn for CDI?

Partners
We work in partnership with our clients and their advisers to meet their evolving needs

Insurance heritage
We leverage this to bring you credible CDI solutions

Experience
We manage £22 billion in buy & maintain credit mandates

A highly regarded credit team
Our strong track record of avoiding downgrades and defaults means we're able to give you more reassurance on your cashflow stability

Our wider asset capabilities
We draw on abrdn's expansive business, including access to illiquid credit and other assets, offering alternativ sources of income

CDI in practice – a case study

We worked with a mature and cashflow negative DB pension scheme which wanted to improve its funding position

- With around £150 million of assets, the scheme was underfunded on a low-risk basis and looking to review its investment strategy.
- It already invested a proportion of assets in bonds – credit and liability-driven investment (LDI) – but there was only minimal income from pooled funds it used.
- To meet benefit payments, the scheme had to regularly disinvest over time.

Key objectives

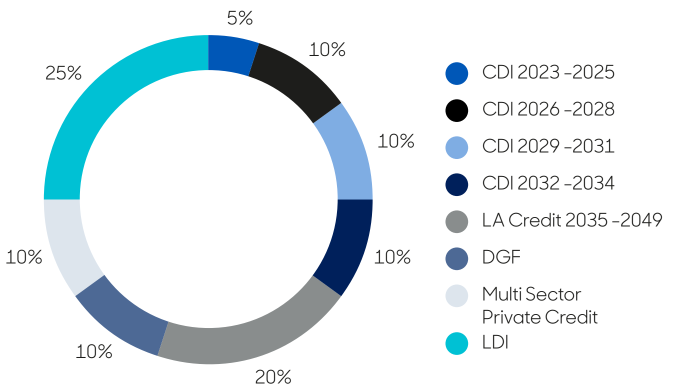
The scheme had two objectives for a new investment strategy:

1. **Close the funding gap –** by achieving sufficient return above gilts.
2. **Limit disinvestment risk –** investing a proportion of assets to provide income that would meet expected future cashflow over the short to medium term

How we found a solution

Working with the scheme's consultant our solution used a combination of four CDI funds, as well as two longer-dated credit funds to broadly match future liability cashflows (as shown in the chart below).

Our analysis suggested that around 55% of the scheme's assets should be invested in the CDI funds. We invested the remaining assets (around 45%) in a range of long-term strategies, including **multi- sector private credit** and **diversified growth** funds. We also included some LDI to hedge a proportion of interest rate and inflation risk.



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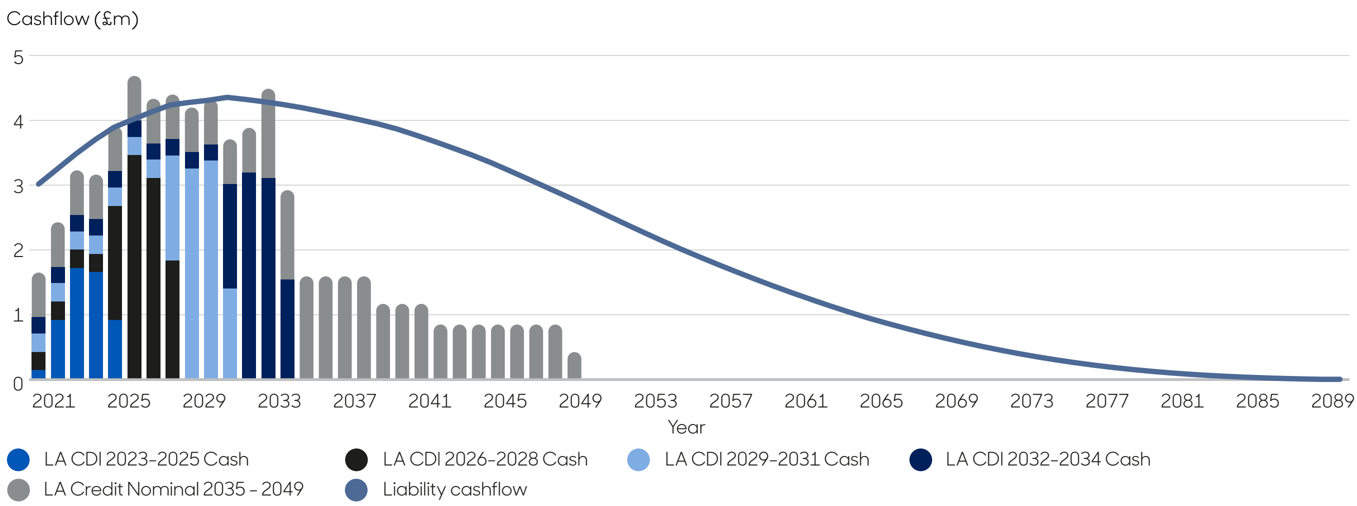

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The result

By matching the first 15 years of cashflow using Liability Aware CDI funds, the client became a genuine long-term investor for the remaining assets, with limited risk of having to disinvest growth assets at short notice.

Over time, as the funding position improves. the scheme expects to switch from growth assets into longer-dated CDI funds.

Key outcomes

- Limited disinvestment / reinvestment risk over the next 15 years as asset income provided to meet future cashflow requirements
- Higher certainty of return from CDI solution compared with typical buy and maintain corporate bond funds
- Genuine long-term investor for growth asset strategies. Low risk of becoming a forced seller of assets

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