BMO Global Asset Management is a leading provider of Liability Driven Investment (LDI) solutions in the UK marketplace with a reputation for innovation and client-focused solutions.

Our equity-linked Dynamic LDI funds provide a solution to the investment needs of UK defined benefit pension schemes in the form of an equity investment that also hedges liabilities.

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Key features

- Capital efficient exposure to liability hedging and global equities in a single pooled vehicle
- Liability hedging employs our popular Dynamic LDI strategy to target outperformance of liabilities
- Futures used to deliver the equity exposure, maximising flexibility and minimising costs
- Full portability with BMO Global Asset Management’s wider LDI fund range

“Combining dynamic liability hedging with synthetic equity exposure is something we have been doing for many years. This innovative solution brings two tried and tested investment approaches together in a straightforward manner, which makes the strategy accessible to pension schemes of all sizes”

Alex Soulsby, Head of Liability Driven Investment

BMO Global Asset Management
The challenge

The majority of pension schemes invest a proportion of their assets in bonds and swaps in order to hedge liability risk. The dilemma for trustees is that this often entails reducing the allocation to growth assets and reduces scope for higher long-term returns. This challenge becomes particularly acute as the hedge ratio rises.

The solution

For every £100 invested, these innovative funds provide £100 of passive synthetic global equity exposure and £200 of liability hedging. This allows investors to hedge liabilities without foregoing equity returns, which are often an essential part of reducing the funding deficit.

The funds combine our tried and tested Dynamic LDI strategy, with global equity exposure delivered using futures, all within a straightforward and governance friendly fund wrapper. The funds form part of BMO Global Asset Management’s extensive LDI fund range, which ensures maximum flexibility for clients. These funds can be combined with other funds in the range to create highly tailored LDI solutions. Additionally, it is easy and cost efficient to switch between these and other funds, for example as a scheme de-risks and reduces its equity allocation or to reflect a changing liability profile.
The hedging part – Dynamic LDI

The hedging component of the funds follow our popular flagship Dynamic LDI strategy and provide hedging across the full maturity spectrum. The liability benchmarks have durations of 24 and 20 years respectively for the Real and Nominal funds, which is in line with a typical UK pension scheme. The funds provide two times leveraged exposure to this benchmark and employ the same robust leverage monitoring and rebalancing process that is applied to our wider LDI fund range. The funds’ liability profiles are illustrated to the right.

The funds employ our Dynamic LDI strategy to target outperformance of the liability benchmark

Yield enhancement
By biasing the allocation towards the cheapest hedging asset, or combination of assets, at each maturity point, we construct a portfolio that exhibits a higher yield than a 50:50 blend of gilts and swaps.

Switching between assets
As the relative price of gilts and swaps changes we gradually sell out of the more expensive asset and buy into the cheaper, higher-yielding asset, resulting in a capital gain.

Important note
This systematic strategy is not dependent on speculative position taking to add value in the same way that a traditional “active” strategy would be.

The equity exposure part – futures

The equity overlay is achieved by investing in a basket of equity futures to reflect a well-diversified global portfolio. The key features of the equity overlay are as follows:

- Use of futures ensures maximum liquidity and minimal dealing costs
- Futures provide a total return i.e. including anticipated dividends
- Collateral pool shared with LDI allocation for efficiency
- Currency exposure is hedged back into sterling
- Regular rebalancing of regional market exposures and overall equity exposure

Target equity exposure

Source: BMO Global Asset Management.

S&P 500  50%
FTSE 100   20%
Eurostoxx 50   15%
Topix   10%
ASX 200  2.5%
Hang Seng  2.5%
Leaders in LDI
The LDI team at BMO Global Asset Management has been at the forefront of innovation in the pooled LDI space since 2006 with a well established track record of being first to market with numerous innovative pooled solutions including equity-linked LDI and Dynamic LDI.

Our innovation, client service and keen focus on risk management has led to us receiving a number of industry awards, listed opposite. This successful framework means we now manage solutions for over 300 clients and have implemented over £346bn in notional derivatives overlay transactions (as at 30 June 2017).

The scale and importance of this capability means that we are committed to the continued growth and reinforcement of the product platform.

Team and resources
Led by Alex Soulsby, the 20-strong team includes derivatives fund managers, quantitative analysts and investment specialists who are experts in derivatives, insurance, pensions, quantitative methods and fund management, with an average of 11 years in the industry. The team is well supported in its activities by the global rates and dealing teams, as well as a deep pool of middle office and client servicing functions. The seamless delivery of investment solutions to our clients is underpinned by a first-class technology and systems infrastructure.

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