



# Pension increases

The HHG Staff Pension Scheme operates a system of guaranteed pension increases. In accordance with the Scheme Rules, pensions in payment were increased by 2.5% on 1 April 2004, except for some members in the Henderson section, who receive increases of 5% per annum. Deferred pensions were increased in line with the relevant Scheme Rules.

## Auditors' report

The Trustee can confirm that Ernst & Young, the Fund's independent auditors, have confirmed that, in their view, the financial statements show a true and fair view of the financial transactions of the Scheme for the year ended 31 December 2004.

## The Trustee and Advisers

The HHG Staff Pension Scheme is managed by a Trustee company called P.A.T. (Pensions) Limited. There are eight directors of P.A.T, of whom three are elected by active members. Member nominated directors are elected every six years and the next round of elections is due no later than December 2007.

### Trustee

P. A. T. (Pensions) Limited

### Trustee Directors

K Jones, FIA, MBA (Chairman)	Deferred Member
J Darkins, BA	Managing Director, Property, Henderson Global Investors
G S Felston, FCII, MBA	Director of Managing Director's Office, Life Services (Member Nominated Director)
R G Holland-Martin	Pensioner Member
M V Jones, B Eng, ACA	Director of Corporate Strategy, HHG PLC
J Marshall-Robb, Chartered FCIPD	Director of Human Resources, Life Services
M J Mauchline, FCII	Pensioner Member (Member Nominated Director)
H Nawaz-Khan, FIA	Deferred member (Member Nominated Director)

### Secretary

L A Williams, MBA, APMI

Head of Staff Pensions

### Actuary

A F M Watson FFA, Watson Wyatt LLP

### Assistant Secretary

A J Yates APMI

Staff Pensions Technical Manager

### Investment Advisers

Hewitt Bacon Woodrow

### Sponsoring Employer

Pearl Assurance Group Holdings Limited (formerly HHG PLC)  
The Pearl Centre, Lynch Wood, Peterborough PE2 6FY

### Auditors

Ernst & Young LLP

### Joint Legal Advisers

Pearl Group Services Limited (formerly HHG Services Limited)  
Richards Butler

### Custodians

BNP Paribas Securities Services

### Investment Managers

Henderson Global Investors  
Fidelity Investments Life Assurance Limited (for the Money Purchase Section only)  
Deutsche Asset Management Life & Pensions Limited, until January 2005 (for the Money Purchase Section only)  
Standard Life Investments Limited, from October 2004 (for the Money Purchase Section only)  
Legal and General Investment Management Limited, from June 2005 (for the Money Purchase Section only)

### Bankers

HSBC Bank PLC

If members have any queries concerning their benefits or would like to receive a copy of the full Report or the revised SIP, they should contact the administration office at: Staff Pensions, The Pearl Centre, Lynch Wood, Peterborough PE2 6FY. Tel 01733 474980 Email: [Staff\\_Pensions@ukls.net](mailto:Staff_Pensions@ukls.net)

# HHG Staff Pension Scheme

(Formerly the AMP UK Staff Pension Scheme)

The Trustee's report to members for the year ended 31 December 2004



# Transfer of benefits to the Henderson Group Pension Scheme and change of Principal Employer



**Following the Chairman's letter of 17 January 2005, explaining the effect of the sale of Life Services to Pearl Group Limited (previously called Life Company Investor Group), the Trustee promised to update members about any changes affecting the Scheme.**

pensioners and deferred members, were transferred to this new Scheme.

The Principal Employer of the HHG Staff Pension Scheme was changed on 13 April 2005 from HHG PLC to Pearl Assurance Group Holdings Limited.

A transfer value was paid to the Henderson Group Pension Scheme on 31 March 2005 and employees of Henderson and Towry Law, together with relevant

The Trustee has received a number of letters from members about these changes, so here we provide answers to some of the most frequently asked questions:

Question	Answer
Did the Trustee Directors take advice before agreeing to the changes?	The Trustee Directors took actuarial and legal advice in a number of areas before reaching agreement with the Company. In addition, they commissioned PriceWaterhouseCoopers LLP (PWC) to undertake an independent investigation into the financial strength of the organisation.
Why is the sale positive for members?	From the information given to the Trustee it appears that Pearl Group Limited wishes to continue to run Pearl Assurance Group Holdings profitably and has long-term business plans supporting this objective. This is positive for members because it ensures an ongoing and supportive Principal Employer.
Will members' benefits be affected?	No. The changes to the Scheme have no impact on the benefits payable from the Scheme.
Can the new company meet the cost of future contributions?	The Trustee received reassurance from the PWC report that Pearl Assurance Group Holdings and its subsidiaries could comfortably meet the required future contributions and also obtained a concession for a rule change to strengthen the Trustee's power to require contributions in the event of a deficit.
How much was the additional funding and how will it be used?	£75 million has been set aside for the HHG Staff Pension Scheme. This may be used by the Trustee to fund a change in investment strategy to reduce the investment risk in the Scheme. The funds will be released if the Trustee demonstrates that additional contributions are required to support such a change.



# Income and expenditure for 2004

**Fund at 1 January 2004: £1,705,051,000**

	Final Salary £'000	Money Purchase £'000	Total £'000
<b>Income for the year</b>			
Contributions	20,823	691	21,514
Transfers in	409		409
Investment income	50,894		50,894
<b>TOTAL</b>	<b>72,126</b>	<b>691</b>	<b>72,817</b>
<b>Expenditure for the year</b>			
Benefits payable	68,183	329	68,512
Transfers out	4,775	1,003	5,778
State Scheme premium payments		181	181
Administrative expenses	1,581		1,581
Investment management expenses	695		695
<b>TOTAL</b>	<b>75,234</b>	<b>1,513</b>	<b>76,747</b>
Income less expenditure	(3,108)	(822)	(3,930)
Change in market value of investments	118,132	3,012	121,144
Net increase in Fund	115,024	2,190	117,214

**Fund at 31 December 2004: £1,822,265,000**



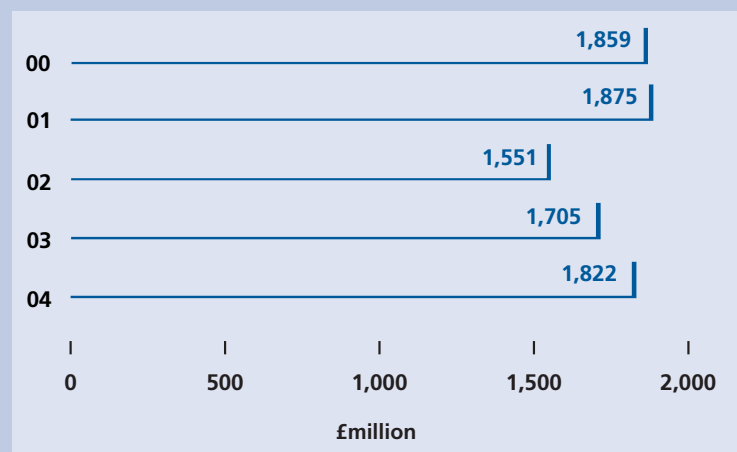
## The financial development of the Scheme

**In 2004 the value of the Fund increased by £117 million. At the end of the financial year to 31 December 2004, the assets of the Fund were valued at £1,822 million.**

An actuarial valuation took place during 2004, based on the position of the Scheme at 31 December 2003. This showed a satisfactory financial position. However, an increased contribution has been recommended for 2005. A major factor of this increase has been the significant reduction in the number of active members, over whom the cost of the administration of the Scheme is currently spread, compared with the numbers of pensioners and deferred members. The new contribution rates will be:

- 27% of pensionable salary for final salary section members
- 13.8% of pensionable salary for pure money purchase section members
- 20.8% of pensionable salaries for hybrid members

**The chart below shows how the value of the Fund has changed over the last five years.**



## Membership

	Final Salary	Money Purchase	Total
<b>TOTAL MEMBERSHIP 1 January 2004</b>	<b>25,783</b>	<b>3,181</b>	<b>28,964</b>
Members in service 1 January 2004	1,401	1,652	3,053
Members in service 31 December 2004	977	1,586	2,563
Pensioners 1 January 2004	8,775	32	8,807
Pensioners 31 December 2004	8,966	45	9,011
Preserved pensions 1 January 2004	15,607	1,497	17,104
Preserved pensions 31 December 2004	15,510	1,777	17,287
<b>TOTAL MEMBERSHIP 31 December 2004</b>	<b>25,453</b>	<b>3,408</b>	<b>28,861</b>

# Managing our investments



Fund	Value	Value	One year performance %
	31.12.2004 £000	31.12.2003 £000	
Henderson Global Equity (Active)	7,248	5,883	9.2
Henderson Global Equity (Passive)	4,610	3,479	11.2
Henderson Mixed Managed	19,884	14,852	7.6
Henderson Global Bond	665	546	1.4
Henderson Index Linked Bond	310	227	9.3
Henderson Cash Fund	476	439	4.0
Henderson Industries of the Future Fund (formerly the Ethical Fund)	74	63	4.2
Henderson Global Technology Fund	40	27	1.5
Deutsche Balanced Fund	1,120	815	8.1
Fidelity Global Equity Fund	2,081	1,519	9.2
Standard Life Managed Fund	9	0	
<b>TOTAL</b>	<b>36,517</b>	<b>27,850</b>	

## Money Purchase Section

Members of the money purchase section can choose to invest in six Henderson funds as well as the Fidelity Global Equity Fund and the Standard Life Managed Fund, which replaced the Deutsche Balanced Fund in January 2005. If a member does not make an investment choice, their credits are invested in the 'default' fund, which is the Henderson Mixed Managed Fund. Members may also choose to invest AVCs in the Henderson Global Technology and Henderson Industries of the Future (formerly the Ethical fund) Funds. The performance of all the funds over the year ended 31 December 2004 is shown in the table above.

## Final Salary Sections

Our investment manager for the final salary section is Henderson Global Investors.

The estimated return for the Scheme for 2004 was 10.6% against the estimated benchmark return of 11.6%. Over the three years to 31 December 2004 the Scheme returned 3.2% per annum against the estimated benchmark return of 4.3%. The poor performance can be attributed in the main to stock selection and Henderson has put in place new structures to address this in 2005.

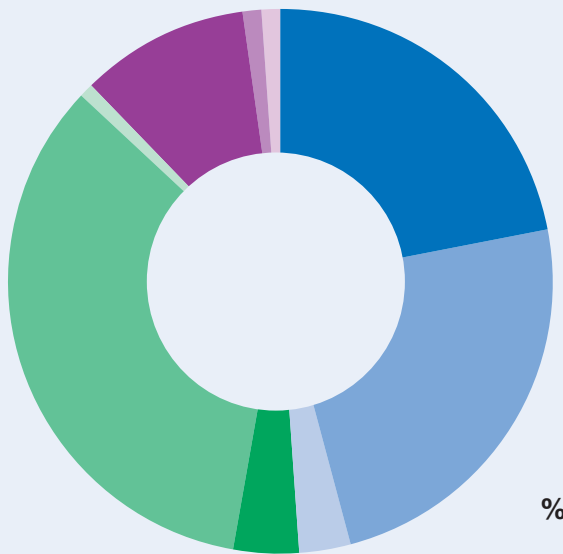
Henderson's summary of market movements in 2004 is shown here.

Equity markets entered 2004 in an upbeat mood. However, during the first quarter of 2004, worries about the US economy grew. Markets drifted lower until mid-August but in the fourth quarter were driven higher, in part by corporate activity in Europe and in the US. In the UK, the FTSE All Share Index rose by 12.84% and the FTSE World Europe ex UK Index registered a 13.83% improvement.

Global government bonds significantly underperformed equities over the 12 month period to 31 December 2004. The JP Morgan Global Government Bond Index rose by 2.7% in sterling terms during the year. US Treasury yields surged in April, as improving employment data seemed to indicate that the economic recovery was under way. The data proved erratic, however, and after peaking at 4.87% in June, ten-year yields sank back to 4.22%. The FTA Government All Stocks Index rose by 6.6% over the period, outperforming other major markets. Index-linked gilts outperformed, returning 8.5%. Corporate bonds also outperformed gilts, with the Merrill Lynch Sterling Non-Gilt Index returning 7.0%.

Currency moves significantly affected returns in overseas markets. The dollar weakened against sterling (-6.8%), the euro (-7.2%) and the yen (-4.3%).

# Asset distribution



● UK equities	22
● International equities	24
● Gilts	3
● Corporate bonds	4
● Index-linked	34
● International bonds	1
● Property	10
● Cash	1
● Other assets	1



## Money Purchase Fidelity Global Equity Fund

The Fidelity Global Equity Fund invests 70% of its assets in UK equities and 30% in overseas equities. Within its mandate is the flexibility to invest up to 20% of the UK portfolio in stocks outside the All Share Index, in non-UK holdings. Fidelity's analysis shows that this would add value to the Fund and as a result they will be using their discretion to invest in this way. The benchmark will remain unchanged, but you may wish to consider whether this changed investment approach would have any impact on your fund choices. If you would like more details about this Fund, please contact Staff Pensions.

## Five largest equity holdings

Holdings	Market Value £m	% of Portfolio
BP	29.5	1.67
Vodafone	29.3	1.65
HSBC	24.0	1.35
Glaxosmithkline	19.1	1.08
HBOS	17.1	0.97

## Money Purchase Global Equity Passive Fund

The Global Equity Passive Fund is currently managed by Henderson. Henderson and the Trustee have agreed that, in future, a passive fund will be provided for the Scheme by Legal and General. Members invested in the Henderson Global Equity Passive Fund have been told of the change and have had their investments switched in accordance with their wishes. Other money purchase members or AVC payers may also wish to consider the new Fund, details of which can be obtained from Staff Pensions.

## Five largest bond holdings

Holdings	Market Value £m	% of Portfolio
UK Treasury 2% index-linked 26/01/35	290.3	16.40
UK Treasury 4.125% index-linked 22/07/30	112.8	6.38
UK Treasury 2.5% index-linked 16/04/20	104.1	5.88
UK Treasury 2.5% index-linked 17/07/24	90.1	5.13
UK Treasury 5% 07/09/14	19.5	1.10



# Statement of Investment Principles

Below is an overview of the Scheme's revised Statement of Investment Principles. It covers both sections of the Scheme.

## Defined Benefit Section

In the current asset allocation strategy, set in February 2005, assets are divided into two categories. First, a portfolio where the assets have similar characteristics to the cash flows of the liabilities, and can consist of a mix of index-linked and conventional bonds (value approximately £700m). Second, a mix of equities, bonds, property, private equity and other assets (value approximately £1.1billion) designed to produce higher returns than the first category.

### Investment objective

The Trustee aims to invest the assets of the Scheme prudently to ensure that the benefits promised to members are provided. In setting investment strategy, the Trustee first considered the lowest risk asset allocation that it could adopt in relation to the Scheme's liabilities. The asset allocation strategy it has selected is designed to achieve a higher return than the lowest risk strategy while maintaining a prudent approach to meeting the Scheme's liabilities.

Since the market value of the Scheme is large compared with the size of the contributions required to fund future service benefits, the Trustee is placing considerable emphasis in its future investment strategy on the reduction of investment risks relative to the liabilities to increase the security of benefits for members. The Trustee therefore aims over time to increase the size of the assets in the first category by reducing the assets in the second.

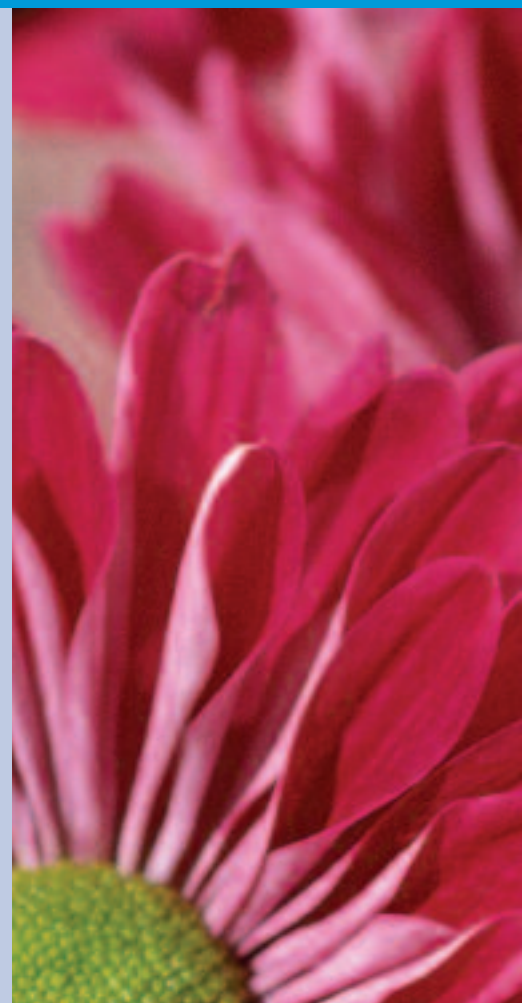
## Money Purchase Section

### Investment objective

In investing the assets of the Scheme in a prudent manner, the Trustee's key aim is to provide a range of investments that are suitable for meeting members' long and short-term investment objectives. They have taken into account members' circumstances, in particular members' attitudes to risk and term to retirement as well as the restrictions in the Trust Deed and Rules on the types of fund that the Trustee can use for employer credits.

The Scheme uses the range of investment options, which the Trustee has selected after taking expert advice from its investment advisers, set out in the table below.

Investment option	Investment description	Aim
Default fund and balanced funds (2 choices)	A diversified portfolio of bonds, equities and property	To provide a return in excess of price inflation and general salary growth
Global equity funds (3 choices)	A mix of UK and overseas equities. A choice of both active and passive management is available	
Specialist equity funds (2 choices for AVCs only)	Funds are available which specialise in ethical investment and technology shares	
Global fixed interest	Fixed interest and corporate bonds	
Index-linked bonds	Index-linked gilts	To broadly match the price of annuities, allowing some protection for members closer to retirement
Cash	Short-term cash instruments	To protect against short-term changes in values for members close to retirement and receiving some tax free cash





These options are provided by Henderson Global Investors, Fidelity Pensions Management and Standard Life Investments Limited.

The structure of the default fund was chosen so as to try to provide a sound expected long-term investment return without undue dependence on a single asset type.

**General investment policy applicable to both sections**

It is the Trustee's policy to consider:

- a full range of asset classes, including alternative asset classes such as private equity
- the risks and rewards of a range of alternative asset allocation strategies
- the suitability of each asset class in the final salary sections' planned asset allocation strategy
- the suitability of each asset class for investment in the money purchase section

- the suitability of the possible styles of investment management and the option of manager diversification for members of the money purchase section
- the need for appropriate diversification both across asset classes and within asset classes

The Trustee's policy is to delegate all day-to-day decisions about the investments that fall within each mandate or fund to the relevant investment manager.

**Governance**

The Trustee is responsible for the investment of the Scheme assets. The Trustee takes some decisions itself and delegates others. The Trustee has established the following decision making structure:

**Structure**



**Trustee**

- set structures and processes for carrying out its role
- select and monitor planned asset allocation
- select direct investments
- decide on
  - selection of investment advisers and fund managers
  - investment structures and their implementation
- monitor investment advisers and fund managers
- monitor direct investments
- make day-to-day decisions relevant to operation of Scheme's investment strategy

**Investment Adviser**

- advise on all aspects of the investment of the Scheme assets, including implementation
- advise on this statement
- provide required training

**Fund Managers**

- operate within the terms of this statement and their written contracts
- select individual investments with regard to their suitability and diversification
- advise Trustee on suitability of its benchmark