January 2012

PENSIONS NEWSLETTER - RBP SUPPLEMENT

For members of the Member Retirement Account (MRA) with Retirement Benefits Plan (RBP) Benefits

Introduction

This supplement to the MRA newsletter is for all those LSM employees who are members of the MRA but who also retain an entitlement under the RBP. It describes matters specific to the RBP; in particular in relation to funding and investment.

The Year in Focus

During the year, the Trustees appointed two new fund managers to better diversify the investment risks of the RBP and more information is provided under the investment section. Some of the key financial highlights of 2010 were:

- The value of the RBP section of the Plan's assets stood at £54.5 million at the year end.
- Company contributions totalling £600,000 were paid into the RBP section.
- Pensions and other benefits paid to members amounted to £2.5 million.

Principal Advisers

In addition to the advisers mentioned in the MRA Newsletter, the Trustees are required to appoint a Scheme Actuary in respect of the RBP section of the Plan. The current Scheme Actuary is Andrew Firbank of JLT Benefit Solutions Ltd.

Investments

Asset Value

The market value of the Plan's assets increased over the accounting year from £51.2 million in December 2009 to £54.5 million as at December 2010. Please note these figures do not include AVC values. Since the year end the value of the fund has increased slightly to £54.76 million as at 30 September 2011.

Investment Performance

The Trustees are committed to monitoring and assessing the performance of the Plan's investment manager. Performance is reviewed at every Trustees meeting and the investment managers are invited to attend Trustee meetings periodically.

The investment return on the RBP's assets for the year ended 31 December 2010 was 10.9% and for the year ended 31 December 2009 was 14.1%, both in line with the index return.

Investment Strategy

Over the year, the Trustees conducted a review of the Plan's investments in conjunction with their investment advisers. The result of this review is that two new investment managers have been introduced to the Plan. The Trustees have disinvested in full the Plan's existing equity holding with Legal & General Investment Management, and invested the proceeds into Baillie Gifford's Diversified Growth Fund, and Standard Life's Global Absolute Return Strategies Fund. Both of these funds aim to give long term investment growth similar to that of equities, but with less short term volatility. This should provide better security for members' benefits, without sacrificing the long term growth that is important to improve the funding of the Plan in the longer term.

The asset transfer took place in August 2011 and therefore details on the performance of the new funds will be provided in next year's newsletter.

How many members?

At 31 December 2010 the RBP had 147 deferred members and 426 pensioners. Comparative figures as at 31 December 2009 are 151 deferred members and 433 pensioners.

A pensioner member is someone who is already in receipt of a pension from the Plan. All of the remaining members of the RBP section of the Plan are deferred members because pensionable service has ceased and no further contributions are payable. Deferred members retain a right to their benefits which will come into payment in the future.

Retirement Options

If you have not already retired you will have the following options when you retire:

- Take your full pension, or
- Take a cash lump sum (currently tax free) and a reduced pension.
- Transfer fund to another pension scheme

Pension Increases

Pensions under the RBP increase on the 15 April each year, at the following rates:

For members who left prior to 6 April 1988:

- 3% per annum for members who left after 6 April 1988
- 5% for service completed prior to 1 January 2000
- In line with the increase in the Retail Prices Index to a maximum of 5% for service completed after 1 January 2000.

Recent Developments

CPI v RPI update

In last year's report we notified members of the government's plans to replace some pension scheme inflation measures that had hitherto been linked to the Retail Prices Index (RPI) with a linkage to the Consumer Prices Index (CPI) instead.

The implications for the benefits payable under the Plan are summarised below:

Pension increases in deferment

The rules of the Plan make provision for some pensions to be protected against inflation in the period from the date pensionable service ceases to the date the pension is put into payment in line with the requirements under pensions legislation. That inflation protection, under pensions legislation, is by reference to RPI for all leavers after the 1 January 1991. If you left the Plan prior to 1 January 1991, the inflation protection is by reference to RPI for periods up to 31 December 2010 and to CPI for periods commencing on or after 1 January 2011.

Increases to pensions once in payment

All pensions accrued prior to 1 January 2000 received fixed 5% per annum increases and are therefore unaffected by the proposed change.

Increases to pensions accrued after 1 January 2000 will continue to be made with reference to RPI.

For the avoidance of doubt if there is any difference between the contents of this report in this respect and the Plan's formal trust deed and rules (as amended from time to time), the latter will prevail.

Ongoing Valuation (including Summary Funding Statement at 31 December 2010)

The Trustees are now able to present the results of the latest funding assessment as at 31 December 2010, and are pleased to report an improvement in the funding position of the Plan since the last formal valuation as at 31 December 2009.

On a continuing basis the funding position of the Plan as at 31 December 2010 (the annual update) and at 31 December 2009 (the formal valuation) was as follows:

Date of assessment	31 December 2010	31 December 2009
Liabilities	£55.5m	£54.5m
Assets	£54.6m	£51.2m
(Shortfall)/Surplus	(£0.9m)	(£3.3m)
Funding level	98%	94%

It is encouraging to see an improvement in the funding position over the twelve months to 31 December 2010. However, the Trustees remain mindful of the impact of global market volatility and economic uncertainty. Even though the Plan's assets increased significantly over 2010, bond yields also fell increasing the value placed on the Plan's liabilities which are measured using bond yields. This offset some of the out-performance experienced on the asset side. In 2011, bond yields have continued to fall and there have also been some significant falls in equity markets. Because of this, the Trustees are realistic about the outcome of the next update due as at 31 December 2011.

The Trustees' prudent investment strategy continues to protect the funding position of the Plan during the sort of volatility we have seen recently.

LSM pays substantial contributions of £50,000 per month to pay off the deficit. It is anticipated that together with future investment returns the deficit will be removed by March 2014. The Trustees acknowledge LSM's ongoing commitment to support the Plan.

Funding Update
You may be aware that the Trustees are required to carry out a formal valuation of the Plan to assess the level of funding on various prescribed bases at least every 3 years. The last statutory valuation was carried out as at 31 December 2009. In the years when a full valuation is not carried out, the Trustees are required to obtain an approximate annual assessment of the Plan's funding position. This approximate assessment is known as the Actuarial Report.

Winding-up Valuation
Legally, we are required to provide members with the following information:

If the Plan had been wound up on the 31 December 2009, there would have been a deficit of around £16.21 million (assuming the assets of the Plan were used to secure members' benefits with an insurance company). The assets would have been sufficient to provide on average 76% of members' full benefits.

This may appear worrying but it is important to understand that, in the first instance, LSM would have been required by legislation to pay a lump sum into the Plan to finance the deficit of £16.21 million, if it were able to do so. If LSM had gone out of business and was not able to pay the amount required to secure the benefits in full, the Pension Protection Fund (PPF), which was established by the Government in April 2005, would provide for a minimum level of benefit. If you would like to know more about the PPF then please visit their website at www.pensionprotectionfund.gov.uk

The fact that we have shown the winding-up position does not mean that LSM is actually thinking of winding-up the Plan.

Payments to LSM
There have never been any payments to LSM out of Plan funds.

The importance of LSM's support
The Trustees' objective is to have enough assets to pay pensions now and in the future. However, success of the funding plan relies on LSM continuing to support the Plan because:

- LSM will be paying the future expenses of running the Plan on an annual basis.
- The funding level can fluctuate and where there is a funding shortfall LSM will usually need to put in more money.
- The target funding level may turn out not to be enough so that LSM may need to put in more money.

Important:
If you are thinking of leaving the Plan for any reason you should always consult a professional advisor, such as an Independent Financial Adviser, before taking any action.

Focus on the Actuarial Valuation Process

Actuarial Valuation

Actuarial valuations of defined benefit schemes (such as the RBP Section of the 2006 Plan) are required at least every three years. These are long and detailed exercises that the Trustees are given 15 months to complete.

An approximate update is required each year between full valuations as well. The Trustees or LSM may call for a valuation at any time.

The main purposes of the valuation are:

- To provide a snapshot of the financial position of the Plan at the valuation date.
- To agree contributions to the Plan and a "recovery plan" if the Plan is not fully funded.
- To comment on the appropriateness of the existing investment strategy.
- To provide the necessary certificates required by legislation.

The calculations
The valuation process involves many hundreds and even thousands of calculations but the calculation of the benefits is effectively carried out in three stages.

1. estimate of the benefit (allowing for adjustment for inflation etc.).
2. allowance for the fact that money set aside today could be expected to grow with interest and so the amount we require today is not as much as would be required to pay the benefit several years in the future.
3. allowance for the probability of the benefit actually being paid.

Employer Covenant

The financial strength of the employer standing behind the pension scheme (particularly defined benefit schemes such as the RBP where there is a funded benefits 'promise') is critical to the valuation process.

The Pensions Regulator requires that trustees of pension schemes which are in deficit should negotiate in the same way as a bank would in dealing with an unsecured debt. In those circumstances, it would be common for a bank to obtain a report on the financial position of the company to assess its creditworthiness. In pensions this is known as an "employer covenant review". This focuses on the financial fundamentals of the business, its balance sheet, cashflow and profits, as well as its future plans and prospects.

An assessment of the covenant ordinarily takes place at the time of the actuarial valuation to assist in considering the appropriate degree of prudence which might be adopted within the assumptions.

For the 2006 Plan, David Beare (the Group Aluminium Business Director) formally updates the Trustees on LSM Group's key financials at least annually. From this and discussions with their advisers, the Trustees 'form a view' of the strength of the covenant for the purposes of their discussions with LSM regarding funding.

Summary RBP Accounts for the Year to 31 December 2010

The following is an extract from the accounts for the year ended 31 December 2010. A full version is available upon request. Figures for the year ended 31 December 2009 are also provided for information.

	2010(£)	2009(£)
VALUE OF THE PLAN AT THE START OF THE YEAR	51,236,992	47,636,966
INCOME		
Contributions:		
Company's:		
Normal	-	-
Special*	600,000	600,000
Members':		
Normal	-	-
Investment Income	75,982	80,028
Transfers in	-	-
Other Income	-	-
Transfers between sections	12,673	93,798
Total Income	**688,655**	**773,826**
EXPENDITURE		
Benefits Payable	2,484,636	3,067,041
Payments to and on account of leavers	-	-
Insurance Premiums	173,244	218,578
Fees and Expenses	163,724	162,677
Total Expenditure	**2,821,604**	**3,448,296**
FUND BALANCE		
Income *less* Expenditure	(2,132,949)	(2,674,470)
Change in Market Value of Investments	5,510,251	6,274,496
VALUE OF THE PLAN AT THE END OF THE YEAR	54,614,294	51,236,992

* Deficit removal payments

Issued on behalf of London & Scandinavian Metallurgical Co Limited, and on behalf of the Trustees of the LSM 2006 Pension Plan
December 2011