DISTRIBUTION GOVERNANCE – MUTUAL ANNUAL REPORTING
DG-MAR: REVIEW - 2023

As part of our Distribution Governance – Mutual Annual Reporting *('DG-MAR')*, this DG-MAR: Review - 2023 explains our ongoing monitoring and review processes and what we identified in respect of the risk / return profiles and expectations of our plans for 2023, focusing on three key areas of consideration:

1) Market risk

2 Issuer and counterparty risk

3) Operational risk

1. Market risk: consideration of any changes to the risk / return profiles and expectations of our plans

Our plans are linked to stock markets, so significant falls in the prevailing level of the stock market index to which the plans are linked and increased stock market volatility have a consequential effect on their prevailing risk / return profiles and expectations. Generally, this can include:

- decreasing the likelihood of the future potential returns (such as kick-out or income payments) being generated; and
- increasing the likelihood of potential capital losses being experienced at maturity.

Global stock markets including the UK bottomed in May 2020 as the world emerged from the Covid-19 lock-down. But the recovery in market was affected by the conflict in Ukraine (Q1 2022), rising inflation and central banks tightening rates rapidly. The gilt crisis triggered by Liz Truss' budget affected the UK financial market briefly in October 2022. Rising rates resulted in a short banking crisis in Q1 2023, where we saw failures of some regional US banks and Credit Suisse. Currently, geo-politics and high rates continued to affect performance of stock and bond markets around the world.

The recovery of the UK stock market in 2021 to 2022 was driven by large cap sectors like energy and oil. This caused a divergence in performance between the FTSE 100 index and the FTSE 100 Equal Weight Fixed Dividend index (FTSE 100 EWFD). This divergence started narrowing in 2023. Over the last 12 months to 29 December 2023 (calendar year end of 2023), the FTSE 100 EWFD index was up 8.92% versus a price return of 3.78% for FTSE 100. But as the table showed, the FTSE 100 EWFD remained lower than that at year end of 2020.

Index	Price return until 29 December 2023		
	1 year	3 years	5 years
FTSE 100 EWFD	8.92%	-0.70%	7.47%
FTSE 100	3.78%	19.70%	14.94%

Source: ft.com

Nevertheless, the better performance of FTSE 100 EWFD over the last 12 months has improved the risk / return profiles of our plans, including those which we highlighted in the last DG-MAR review. The indicative secondary market prices for structured product plans which started in 2021 and 2022 recovered gradually. Some of them remained below £1, reflecting the fact that these plans may not kick out on the first kick out date (usually the 3rd anniversary).

Remember that a delay in kick out does not mean the plans perform differently from the expected outcome when they were launched. Investors in structured product plans are generally expected to be prepared to hold their investments through the investment term, depending on specific plan features. Bid prices / plan values can usually be expected to move towards the stated terms of plans, which are contractually / legally defined on predefined dates. Investors should receive a positive return when a kick out occurs that could beat the performance of passive index funds over the same period. 38 of long kick out our plans have achieved early maturity since Tempo started launching products. 35 of them kicked out at the earliest kick out date (third anniversary), and 3 kicked out at end of year four. 27 of them performed better than a FTSE 100 index fund.

Furthermore, our long income plans continue to pay out income every quarter thanks to the defensive design of our products for end investors in uncertain markets.

Despite possible headwinds in the stock markets, the nature of our structured product and structured deposit plans should continue to deliver the intended outcome for investors, and the market conditions have not affected the return objectives and risk profile of our plans.

In summary, over the period of review:

i) we identified how the improved economic prospects and stock market performance affected the prevailing risk / return profiles and secondary market prices of our plans;

ii) since our last DG-MAR review, we did not identify any plans which were performing differently to their known features and expected outcomes, in respect of market risk, and this has remained the case as markets continued to recover;

iii) we did not identify any plans which had become inconsistent with the needs, characteristics and objectives of our identified target markets; and

iv)) we did not identify any need for professional advisers (or end clients) to take any specific action in addition to their regular and ongoing review of the suitability of portfolios for individual client circumstances.

2. Issuer and counterparty risk: consideration of any changes to the risk / return profiles and expectations of our plans

Both the potential returns of our plans and the repayment of money invested depend on the financial stability of the issuer and counterparty bank for each plan. If the issuer and counterparty bank for a plan become insolvent, or similar, or fail to be able to meet their obligations, it is likely that end clients will receive back less than they invested.

One measure of the credit strength is credit default swap (CDS) levels. We monitor them under the CDS category in our Tempo Issuer and Counterparty Scorecards (TICS). Banks' CDS fell over 2020 and 2021 due to improving prospects of the end of the Covid-19 pandemic. But rising inflation prompted central banks including the Bank of England to start raising interest rates in early 2022. Banks CDS started to rise as concerns grew on the impact of such *'quantitative tightening'*. In Q1 2023, the rise in bond yield (and corresponding fall in value of government bonds held by banks) resulted in failures of a few US regional banks like the Silicon Valley Bank (SVB). That triggered deposit flights with some weaker banks, including Credit Suisse. Authorities around the world stepped in. Credit Suisse was eventually taken over by UBS.

The average TICS score under the CDS category stayed high in 2022 (as per the approach for all of our TICS Category Scorecards, the scoring system is based on a score out of 10, where a low score is good for credit risk versus a high score). It improved over 2023 in spite of the short banking crisis, and the average stood below 5 (out of the highest *'bad'* score of 10) at December 2023.

Meanwhile, banks' earnings held up and their balance sheets remained strong in 2023. The average TICS Fundamental scores stayed largely unchanged (Balance Sheet) or improved (Market Indicators). The average TICS overall score was close to that at end of 2020.

Based on these metrics, we concluded that despite the stress in Q1 2023, the issuer and counterparty credit risk remained largely unchanged over the period of review.

	TICS Credit Score (average)	TICS CDS Score (average)	TICS Fundamentals (Balance sheet) Score (average)	TICS Fundamentals (Market Indicators) Score (average)	TICS Systemic Importance Score (average)	TICS Overall Score (average)
December 2023	6.11	4.85	4.19	4.95	4.37	517.18
December 2022	6.12	5.69	4.04	5.12	4.35	525.29
December 2021	6.15	3.63	4.08	4.88	4.35	498.20
December 2020	6.28	3.52	4.19	5.64	4.41	512.72
June 2020	6.23	5.17	4.15	5.82	4.42	533.73

(For more details about our TICS methodology, see here: https://tempo-sp.com/tics)

With regard to credit ratings of counterparties specific to our structured product and structured deposit plans, on 3 July 2023 Fitch Ratings raised the outlook for Societe Generale's long term rating to positive from stable (simultaneously affirming an 'A-' rating). There has been no change in the credit ratings for Royal Bank of Canada, which is the other deposit taking bank for our structured deposits.

In summary, over the period of review:

i) **we identified how the current interest rate and economic environment affected the prevailing issuer and counterparty risk profiles of our plans;**

ii) **since our last DG-MAR review, we did not identify any plans which were performing differently to their known features and expected outcomes, in respect of issuer and counterparty risk;**

iii) **we did not identify any plans which had become inconsistent with the needs, characteristics and objectives of our identified target markets; and**

iv) **we did not identify any need for professional advisers (or end clients) to take any specific action in addition to their regular and ongoing review of the suitability of portfolios for individual client circumstances.**

3. Operational Risk: consideration of any changes to the risk / return profiles and expectations of our plans

Tempo Structured Products *('Tempo')* is part of the Alpha Real Capital family of companies *('Alpha')*.

As we emerged from the Covid-19 pandemic, Tempo, the wider Alpha family and our plan administrator, James Brearley & Sons *('JBS')*, continued to do well both operationally and financially. With our strong performance, at the end of 2022 Tempo applied to the Financial Conduct Authority to become a directly authorised firm. We received the approval on 08 December 2023 and Tempo is now directly authorised. This positive development in our regulatory status will be key for our growth plan as we continue to strengthen our team with new hires and products.

JBS continued to experience a growth in trading volumes across their whole business over the review period. It continued to meet all service level agreements and key performance indicators with Tempo.

The COVID-19 lock-down changed how many people work and how businesses operate. We recognise that technology has become more important in our industry, with more professional advisers embracing online, digital ways to doing business. We continued to interface with professional advisers with Teams, Zoom and other online communication options. Our live video webinars continued, covering new products (including our structured deposits and fixed rate deposits) and different topics in structured investments.

In summary, over the period of review:

i) we identified how the improved operational risk prospects affected the prevailing risk / return profiles of our plans;

ii) since our last DG-MAR review, we did not identify any plans which were performing differently to their known features and expected outcomes, in respect of operational risk;

iii) we did not identify any plans which had become inconsistent with the needs, characteristics and objectives of our identified target markets; and

iv) we did not identify any need for professional advisers (or end clients) to take any specific action in addition to their regular and ongoing review of the suitability of portfolios for individual client circumstances.