AGENDA ITEM 12

FALKIRK COUNCIL

Subject: **FUND MANAGER PERFORMANCE REVIEW**
Meeting: **PENSIONS COMMITTEE**
Date: **12 DECEMBER 2013**
Author: **CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 The Local Government Pension Scheme Regulations require that Falkirk Council, as administering authority for the Pension Fund, review the investments of its Managers at least once every three months, which includes an analysis of returns and risk. This paper reports on performance for the overall Fund and on fund manager reviews.

1.2 The rates of return achieved by our Fund Managers are measured against pre-determined benchmarks. This service is provided by the Fund's custodian, Northern Trust.

1.3 The undernoted benchmarks are in place to measure the performance of each Manager.

Fund Manager	Benchmark
Aberdeen Asset Management (AAM)	MSCI All Countries World Index
Baillie Gifford Bonds (BGB)	Customised benchmark comprising UK Fixed Interest and UK Index Linked Bonds
Baillie Gifford Diversified Growth (BGDG)	UK base rate
Legal & General (L&G)	Customised benchmark comprising UK and Overseas Equities
Newton Investment Management (NIM)	FTSE All World Index
Schroder Investment Management (SIM) UK Equities	FTSE All Share Index
Schroder Investment Management (SIM) Property	HSBC/APUT Pooled Property Fund Indices

1.4 Full details of each Manager's portfolio activity and any engagement with companies on corporate governance issues are recorded in their individual quarterly investment reports, which are enclosed.

2. MARKET REVIEW AND OUTLOOK

2.1 Global equity and bond markets recovered well in the third quarter from the considerable buffeting they had received in early summer when investors became unsettled by the prospect of QE tapering in the USA, and by concerns around growth prospects in China. Central bankers in the main developed markets sent a similar message to investors as the one delivered by new Governor of the Bank of England, Mark Carney, at his first policy meeting in July – the Bank remains in policy loosening mode, which supports asset prices. Chinese economic data too showed signs of stabilisation, which allayed earlier fears.

2.2 For UK investors, the extent of the recovery in asset prices was muted by sterling strength in the quarter – it rose by approximately 6% against the dollar and 3% against the Euro. UK real GDP growth rose +0.7% in the second quarter, and for the first time in almost three years, all sectors of the economy (services, production, construction and agriculture) made a positive contribution to growth. Signs of a stabilisation in Euro area activity in recent months have also encouraged improving confidence in the macro economic outlook. The quarter saw particular strength in the share prices of smaller companies in the UK and those in the peripheral European markets which have been most challenged by the European recession, such as Greece and Spain.

2.3 Further afield, in Japan, the economy continued to show signs of life following the shift towards an easier monetary policy stance earlier in the year. The Upper House elections gave control of both houses to Prime Minister Abe, giving him the freedom to push ahead with his third policy "arrow" – structural reforms. In addition, Tokyo won the competition to host the 2020 Summer Olympics, which will boost economic activity in the intermediate term.

2.4 Against a backdrop of modestly improving economic growth and subdued inflationary pressures across the developed world, monetary policy is set to remain accommodative into 2014. The US economy continues to lead the developed markets pack in growth terms, though the economy is still only growing around a 2% annualised rate. The environment appears to be supportive for asset prices, but increasingly, asset managers are nervous that equity markets are becoming expensive and that when tapering of quantitative easing occurs, there will be a nasty hangover. What seems likely is that the recent rate of appreciation in equities (+22% over the last 12 months) will slow when tighter monetary policy becomes a reality.

3. ANALYSIS OF PERFORMANCE RESULTS

3.1 The total fund and individual external manager returns are shown in the table in Appendix 1. The returns for the quarter ending 30 September 2013 are shown, but this is a very short period to measure performance. It simply reflects the regular reporting cycle. Each manager has been set its own individual investment objective, which depends on the type of mandate awarded. Each active manager is tasked with outperforming its benchmark over either three or five year periods. The table in Appendix 1 incorporates the relevant return and benchmark data and the excess return relative to the manager's benchmark and outperformance objective. More detail on individual manager mandates and objectives can be found in Appendix 2.

3.2 Although bond and equity markets rebounded from their summer lows, there was a significant divergence in performance. Within equities, UK and European returns were best in the mid to high single digits while North American and Emerging Market returns were negative in sterling terms. Fixed income bond returns were positive while index-linked gilts fell slightly. UK property markets firmed with evidence of the recovery broadening.

3.3 The overall Fund's return of +2% over the quarter was in line with the benchmark return. Over the 3 year period, the Fund benefited from a significant recovery in equity markets rising +9.7% per annum compared with the benchmark return of +7.8% per annum, an excess return of +1.9% per annum. Long term return data shows Fund appreciation of +10.0% per annum over 5 years and +7.1% per annum since September 2001. These long term returns are above the benchmark returns.

3.4 Over the third quarter of 2013, the Fund's three active equity managers posted returns from +0.2% to +8.1%. Only SIM managed to beat its benchmark, while AAM and NIM lagged their respective benchmarks. The Fund's passive equity manager, L&G, produced a return of +2.7%, in line with its benchmark return, and so consistent with its mandate.

BG's bond mandate returned +1.2%, which was 0.1% behind its benchmark return. BG's other mandate, the Diversified Growth portfolio, rose 1.1%, which was ahead of its benchmark by 1.0%.

The property portfolio managed by SIM lagged its benchmark by 0.3%, but rose 2.1% in absolute terms.

3.5 Longer term return data shows that SIM's UK equity portfolio is comfortably ahead of its objective of +1.25% per annum above the benchmark over the 3 year period and since inception.

NIM's global equity mandate stipulates an objective of +3% per annum over 5 year rolling periods. Returns over the past 3 years, 5 years and since inception have beaten the benchmark. Since inception in June 2006, returns are ahead of benchmark by 1.1%, so NIM has added value, but it has not achieved its objective.

The AAM mandate's objective is +3% per annum outperformance over 3 year rolling periods. Performance is ahead of benchmark, but lagging the objective. After an excellent start to the mandate, the last 12 months performance has detracted from relative returns, which are ahead of benchmark by 1.3% per annum since inception in May 2010.

The performance of BG's bond mandate is lagging its benchmark by 0.4% per annum since inception in 2007, but the 3 year performance has been very strong. The excess return over the benchmark of +1.4% per annum comfortably exceeds the objective of +0.9% per annum over rolling 3 year periods.

SIM's property performance has been disappointing in recent years, and this has reversed positive results in the early years of the mandate. Since inception in 2005, a period of low returns for commercial property owners, the portfolio has performed more or less in line with its benchmark.

4. CONCLUSION

4.1 Following a nervous end to the previous quarter, global markets were buoyed by improving macro-economic data and by the continuation of accommodative monetary policy. A common feature was concern from Asset Managers that markets were becoming over valued.

4.2 Over the quarter the Fund value increased by 2% marginally behind the benchmark return of 2.1%. Currency exposure and defensive positions held by the Fund's Global Equity managers resulted in a slight drag in performance against benchmark. Schroder's UK Equities has once again continued to perform comfortably above benchmark.

5. RECOMMENDATIONS

5.1 The Committee is asked to note:-

(i) the Manager's performance for the period ending 30 September 2013; and

(ii) the action taken by Managers during the quarter to 30 September 2013 in accordance with their investment policies.

Chief Finance Officer

Date: 28 November 2013

Contact Officer: Alastair McGirr, Pensions Manager, Tel: 01324 506304

LIST OF BACKGROUND PAPERS

1. The Northern Trust Company – Fund Analytics 30 September 2013

Any person wishing to inspect the background papers listed above should telephone Falkirk 01324 506304 and ask for Alastair McGirr

APPENDIX 1 – PERFORMANCE MEASUREMENT (RATES OF RETURN)

Rates of Return by Manager with Excess Returns - 30 September 2013								
			Returns					
Manager	**Market Value £**	**Weight**	**3 months**	**3 year**	**5 year**	**Since inception**	**Inception Date**
Aberdeen Portfolio	204,418,064	13.8%	0.3%	10.6%	-	9.5%	May-10
Benchmark			1.2%	9.8%	-	8.2%	
Excess Versus Benchmark			**-0.9%**	**0.8%**	**-**	**1.3%**	
Excess Versus Objective			**-**	-2.2%	**-**	-1.7%	
Baillie Gifford Bond Portfolio	131,445,112	8.9%	1.2%	7.4%	8.7%	6.2%	Mar-07
Benchmark			1.3%	6.1%	7.7%	6.6%	
Excess Versus Benchmark			**-0.1%**	**1.4%**	**0.9%**	**-0.4%**	
Excess Versus Objective				**0.5%**	**0.0%**	**-1.3%**	
Baillie Gifford Diversified Growth	140,535,771	9.5%	1.1%	-	-	6.9%	Feb-12
Benchmark			0.1%	-	-	0.5%	
Excess Versus Benchmark			**1.0%**	**-**	**-**	**6.4%**	
Excess Versus Objective *			**-**	**-**	**-**	2.9%	
Legal & General	311,331,683	21.0%	2.7%	10.3%	-	15.1%	Jan-09
Benchmark			2.7%	10.3%	-	14.9%	
Excess Versus Benchmark			**0.1%**	**0.1%**	**-**	**0.1%**	
Excess Versus Objective			**-**	**0.1%**	**-**	**0.1%**	
Newton	215,321,877	14.5%	0.2%	10.5%	11.6%	8.3%	Jun-06
Benchmark			1.2%	9.7%	10.5%	7.2%	
Excess Versus Benchmark			**-1.0%**	**0.9%**	**1.1%**	**1.1%**	
Excess Versus Objective			**-**	**-**	**-1.9%**	**-1.9%**	
Schroders UK Equity	252,559,250	17.0%	8.1%	14.7%	15.6%	9.6%	Sep-01
Benchmark			5.6%	10.1%	10.7%	7.0%	
Excess Versus Benchmark			**2.5%**	**4.6%**	**4.9%**	**2.6%**	
Excess Versus Objective			**-**	**3.3%**	**3.7%**	**1.3%**	
Schroders Property	104,796,736	7.1%	2.1%	3.6%	0.2%	1.0%	Nov-05
Benchmark			2.4%	4.6%	1.3%	0.8%	
Excess Versus Benchmark			**-0.3%**	**-1.0%**	**-1.1%**	**0.2%**	
Excess Versus Objective			**-**	**-1.7%**	**-1.8%**	**-0.6%**	
Total Fund	1,483,560,018	100.0%	2.0%	9.7%	10.0%	7.1%	Sep-01
Benchmark			2.1%	7.8%	8.5%	6.8%	
Excess Return			**0.0%**	**1.9%**	**1.5%**	**0.3%**	

*** Note that objectives are set over 3 or 5 year periods and Baillie Gifford's Diversified Growth mandate has not been in place for the requisite periods.**

There are small rounding effects in the table above.

APPENDIX 2 - INVESTMENT MANAGER COMMENTS

Aberdeen Global Equity

(13.8% of Total Fund)

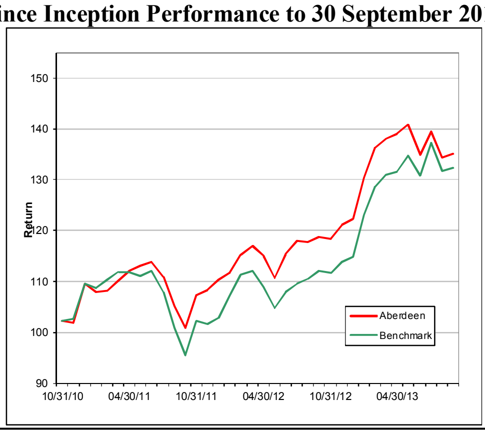
Investment Approach:

High conviction, research-driven house. Only invest in companies they have met. Regional teams produce Global buy list of 330 stocks. Global team carries out comparative analysis and produces model portfolio of 50 stocks from which team must build portfolio. Long-term horizon, trading highly price-sensitive.

Investment Objective:

To outperform the MSCI AC World Index in sterling by 3% per annum, gross of fees, over rolling 3 year periods (inception date 16 May 2010

Since Inception Performance to 30 September 2013



Q3 2013	: -0.9% excess return
3 Years	: +0.8% excess return
Since inception	: +1.3% p.a. excess return *
	(* +1.8% Aberdeen figures)

Summary

Performance history is short - beating benchmark, but behind objective, since inception. Short term (12 month) performance is weak (-4.1% rel), due mainly to defensive sector positioning and poor stock selection within financials.

Portfolio

The portfolio is genuinely unconstrained, which indicates that it should be able to achieve its objectives. No single investment more than 5% of the portfolio is allowed, but sector and country limits are wide (+/-15% for sectors and +/-35% for countries allowed). Cash currently at 1.5%.

The portfolio is more geographically diverse than the benchmark. North America represents >50% of the benchmark, but the portfolio is u/w by more than 20%. The fund is o/w the UK (+10%), Europe ex-UK (+6%), and LatAm (+6%). By sector, the portfolio remains heavily o/w defensive sectors, such as consumer staples (+5%), energy (+3%) and healthcare (+3%), and has low exposure to cyclical earnings, such as consumer discretionary shares (-10%) and industrials (-2%). Consequently, the portfolio is likely to perform relatively poorly in strong equity markets, but its defensive tilt should help protect it in the event of equity markets falling. Aberdeen has a little more in cyclicals/less in defensives than in the recent past, but the portfolio remains defensive and the house view remains very cautious, especially now developed markets have risen so much. Aberdeen think removing the QE stimulus will be a real challenge for markets.

Performance was behind the benchmark as a result of negative stock selection in Asia Pacific (Taiwan semi), Canada (Potash Corp), Europe (Zurich Insurance) and Japan (Shin-Etsu chemical), particularly in the materials and IT sectors. There was positive performance from energy (EOG Resources, Schlumberger) and telecoms (Vodafone) stock picking. Allocation to countries was positive (mainly o/w UK, u/w US), though allocation to sectors was negative, with the overweight in consumer staples and underweight in consumer discretionary again detracting from performance.

Turnover remains low. A new position was taken in South African telecoms provider MTN Group due to its attractive growth profile, strong cash flow generation and dividend growth potential. The position in Japanese optical giant Canon was sold outright. Aberdeen added to existing positions in Banco Bradesco, Petrochina, Petrobras, Potash, Shin-Etsu Chemical, Baxter International and FEMSA on weakness and/or cheap valuations. Holdings in Tenaris, Nestle and Vodafone were reduced on strength. Aberdeen remains very cautious, believing that unconventional monetary policy measures are masking a much worse economic backdrop than headline numbers suggest. Share buybacks have been a disproportionate driver of earnings growth and markets have risen largely on the back of multiple expansion.

Key considerations/developments

Ownership has not changed but company acquired Artio Global Investors and a 50.1% stake in SVG Advisers in May 2013, and are rumoured to be about to bid for SWIP; the **client base** is stable (though -£686m in Q3 with 1 net client lost) and the **investment process** has not changed/is standardised across all equity products. This facilitates cross-fertilization of ideas and a team-led approach. Stable, well-resourced and very experienced **investment team** (6 most senior team members average >19 years in industry and >12 years at Aberdeen), backed up by extensive and very experienced regional teams.

Baillie Gifford Bonds

(8.9% of Total Fund)

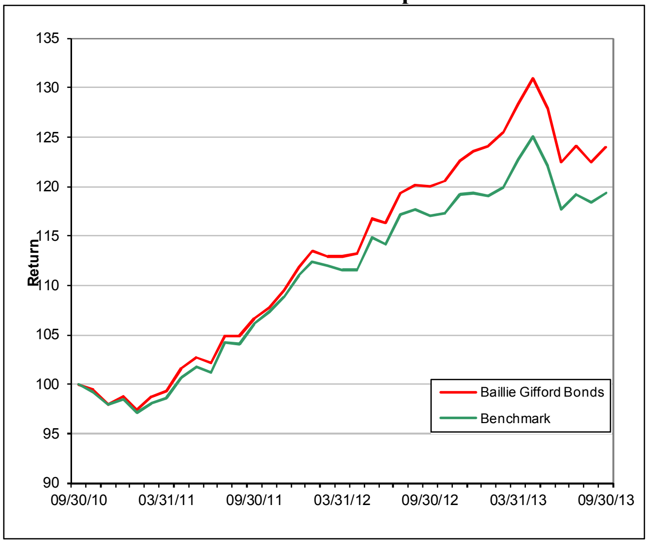
Investment Approach:

Baillie Gifford employs fundamental analysis to identify sustainable trends. It believes that there are inefficiencies that can be exploited in the areas of stock selection and interest rate and currency strategies.

Investment Objective:

To outperform a customised benchmark comprising index-linked gilts, conventional gilts and investment grade bonds by 0.9% per annum net of fees over rolling 3 year periods (inception date 30 March 2007).

3 Year Performance to 30 September 2013



Q3 2013	: - 0.1% excess return
3 Year	: + 1.4% p.a. excess return
Since inception	: - 0.4% p.a. excess return

Summary

3 year performance is well ahead of the objective.

Portfolio

The portfolio has a customised benchmark (20% FT-Actuaries Over 5 Years Index Linked Gilt Index, 30% FT-Actuaries All Gilts, 50% Merrill Lynch Sterling Non-Gilt Index). Baillie Gifford (BG) invests in three BG Funds on a no-fees basis to achieve the appropriate exposure. The current benchmark was set in 2009 when the view was taken that a greater exposure to Credit was appropriate.

Over the quarter, corporate bonds gained +2.2% while conventional and index-linked gilts both gained +0.5%, meaning that the 20/30/50 benchmark performed better than the pre-2009 20/40/40 benchmark.

The Portfolio has maintained its relatively small (3 to 4%) overweight position in Corporate Bonds relative to Gilts, and BG is maintaining the overweight position in EM issuers and currencies. Holdings denominated in foreign currency remained at 8.2% of the fund (benchmark 0%), but these positions are hedged back to sterling.

Given an improving macroeconomic backdrop, the portfolio reflects a positive view on ‘BBB’ rated bonds (22.4% vs benchmark of 16.2%) and High Yield (4.3% vs 0%). Secured senior debt is also favoured.

The small under performance over the quarter was due to: a) asset allocation – overweight in emerging markets (EM), particularly Brazil, Mexico and Russia, which lagged UK Bonds; b) currency - overweight currency positions in EM economies also had a negative effect. The threat of US tapering of QE continued to weigh on EM. Over 12 months, the portfolio is +1.0% relative to the benchmark, mainly due to stock selection.

Key considerations/developments

BG is a long established, reputable partnership; the client base is stable and the investment process has not changed. While the 3 co-managers remained the same, there was a rotation in the investment graduates supporting the mandate, which is part of the firm’s normal development programme. Assets under management in the strategy were down slightly to £1.2bn across 11 clients.

Baillie Gifford Diversified Growth

(9.5% of Total Fund)

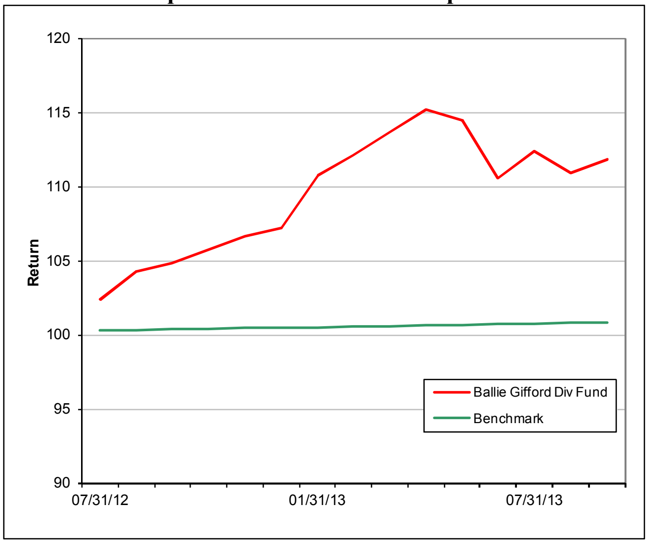
Investment Approach:

Baillie Gifford invests in a broad range of traditional and alternative asset classes, such as equities, bonds, property, private equity, infrastructure, commodities and currencies, adjusting portfolio weightings to reflect the relative attractiveness of the individual assets.

Investment Objective:

Objective: to outperform the UK base rate by at least 3.5% per annum (after fees) over rolling five year periods with an annual volatility of less than 10%. (Inception date 2 February 2012)

Since Inception Performance to 30 September 2013



Q3 2013	: +1.0% relative to base rate
1 Year	: +6.2% relative to base rate
Since inception	: +6.4% pa relative to base rate

Summary

Falkirk has been invested since Feb 2012. The risk/return is beating the fund objectives (4% pa return with less than 10% volatility) with 6.9% pa return and 7.1% volatility.

Portfolio

The portfolio consists of a range of 15 asset classes, which is designed to protect the portfolio from the volatility experienced by equity investors. The portfolio's largest exposure is, in fact, listed equities (18.2%) with listed private equity a further 3.5%. BG's risk analysis shows that these allocations contributed 3% and 1% respectively of the total 7% volatility. In the third quarter, listed equities contributed 1.2% to performance meaning everything else netted out to a slight negative.

Other significant exposures are emerging market debt (15%) and high yield bonds (11.5%). Cash has now been reduced to 6% (from 15% in 2012).

The listed equities exposure is mainly through stakes in BG funds: Global Alpha (6.0%), Global Income (5.8%), Long Term Global Growth (2.0%) and Japan (0.2%). Local currency emerging market debt exposure is mainly held through the BG Emerging Markets Bond Fund (9.7%). Cash exposure is through BG Worldwide Cash Plus Fund (2.5%). Other BG fund holdings are BG High Yield Bonds (5.5%) and BG Worldwide Credit (7.2%). These fund holdings make up 39% of the portfolio. Each fund has a different benchmark and objective to Diversified Growth, which may cause contradictions and add to risk (eg currency positions).

The current predicted volatility is now 7.1% - over half of which is from (listed and private) equities. Targeted maximum volatility is 10%, which compares with 17.1% for global equities.

Key considerations/developments

Baillie Gifford is a long established, reputable partnership. The **assets** in this product increased over Q3 to £4.4bn, with another £0.25bn inflow (same as Q2). Despite being closed to "all new clients" from end June 2013, client numbers rose over Q3 by 8 (9 won and 1 lost) to 233. The **investment process and team** has not changed. The 39% invested in other Baillie Gifford funds have zero fees but still pay expense. The c1/3rd invested in other manager's funds bear double-charging.

Newton Global Thematic Equity

(14.5% of Total Fund)

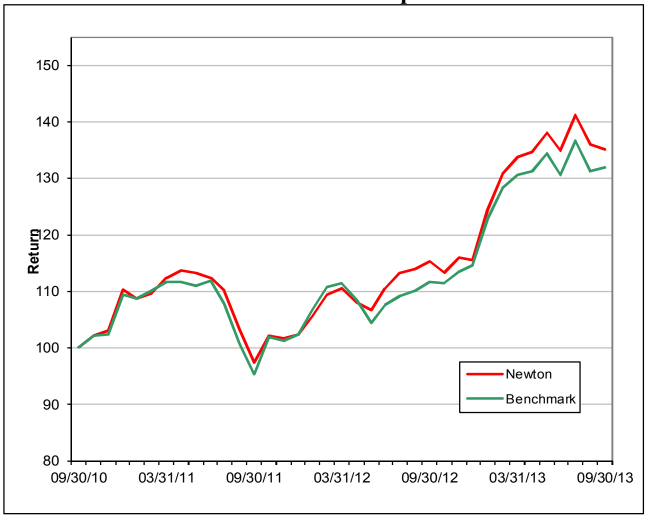
Investment Approach:

Newton identifies structural trends to gain perspective on the important risks and opportunities in investment markets. This thematic framework drives stock selection, which results in a concentrated portfolio.

Investment Objective:

To outperform FTSE All World Index by 3% per annum (net of fees) over rolling 5 year periods (inception date 30 June 2006)

3 Year Performance to 30 September 2013



Q3 2013	: - 1.0% excess return
5 Years	: + 1.1% p.a. excess return
Since inception	: + 1.1% p.a. excess return

Summary

	Portfolio not achieving objective, but is ahead of benchmark since inception.

Portfolio

The portfolio is genuinely unconstrained (49 stocks), indicating that it should be able to achieve its objectives. This is an equity portfolio, but the manager is able to hold up to 10% in cash. The manager continues to take a defensive stance and cash (including short term US Treasuries) was 9.7% at quarter end.

Flowing from Newton's themes, which include deleveraging, financial concentration and growing Chinese influence, the portfolio is characterised by companies with stable earnings, strong cash flow, competitive advantage, inflation linkage, innovation, exposure to growth economies, good management & governance and attractive valuation.

The portfolio has high exposure to companies in the healthcare, staples, food producers and tobacco sectors, while financials, industrials, oil and gas and consumer services companies with cyclical earnings are under-represented (though o/w materials). The portfolio is likely to perform relatively poorly during strong equity markets (especially given the 10% cash position), but its defensive tilt should protect it to some extent in the event of equity markets falling. Portfolio is overweight Europe (+14%) and UK (+2%) equities, and underweight North America (-7%), Japan (-6%), Pacific (-5%) and other/emerging markets.

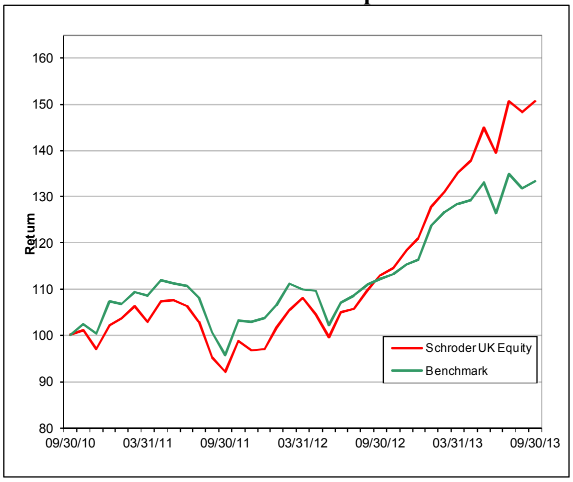
Q3 performance was hit by the high (US$) cash (and equivalents) level in the portfolio, as the US$ weakened relative to £. Stock picks within healthcare (Fresenius, Lab Corp) and industrials (Xylem, Accenture) were the main negative drivers. This was partially offset by positive stock picking in consumer services (Reed Elsevier) and energy (Suncor, Total).

The manager added four new stocks in Q3: Newcrest Mining was switched into rival Yamana Gold (better asset quality/balance sheet, superior production growth); Citigroup (cheap valuation, improved profitability and risk controls); Toymaker Mattel has strong opportunities in EM, and should benefit from the convergence of toys, media & entertainment as well as having strong cash flow characteristics and balance sheet; Walt Disney should benefit from earnings growth as capex at its resorts pays off, while ESPN sports and Star Wars franchises should see growth and improved returns. There were outright sales of oil group Petrobras (headwinds from Brazilian government's fuel price policy), construction group Bilfinger, Xylem (disappointing results and near term growth risks) and defence group Flir Systems (valuation).

Key considerations/developments
Newton remains one of Bank of New York Mellon's asset management subsidiaries based in London; in the face of weak relative returns, management reassessed the **investment process** in 2011/12 and made some personnel changes to improve rigour, but did so without changing the key elements of the global thematic strategy; the **client base** is stable (1 new client in Q3 with £31m net inflow).

Schroders UK Equity
(17.0% of Total Fund)

3 Year Performance to 30 September 2013



Investment Approach:

Schroder seek to identify stocks which trade at a substantial discount to their intrinsic value and where they believe that profits will surpass expectations. The investment style can be categorised as "value".

Investment Objective:

To outperform FTSE All Share Index by 1.25% per annum (net of fees) over 3 year rolling periods (inception date 31 March 2007)

Q3 2013	: +2.5% excess return
3 Year	: +4.6% p.a. excess return
Since inception	: +2.6% p.a. excess return

Summary

Further strong performance in Q3 on both an absolute and relative basis with manager comfortably ahead of the objective on all timeframes. Clearly articulated strategy with stable ownership, client base and investment team.

Portfolio

The portfolio of 43 stocks deviates from the benchmark meaningfully, which means that the objective should be achievable, but the return profile is likely to be highly variable.

Active sector positions are relatively unchanged from last quarter. The portfolio retains a zero weight in basic materials and a zero weight in utilities. Overweight positions include general retailers and life insurance. The portfolio has a cyclical bias as this is the area of the market that provides the value opportunity.

Relative returns in the third quarter were strong (+2.5%). The portfolio has gained 33.5% over the last 12 months versus an index up 18.9%. The portfolio benefited from exposure to companies such as RBOS, Rentokil, Resolution and Home Retail which all outperformed significantly.

Existing holdings where valuations remain attractive have been increased, notably in a number of banking and financial related stocks. A small new position was taken in W&G Investments, a vehicle created to bid for part of the RBS UK retail branch network. Having been unsuccessful in the auction, roughly two thirds of monies will be returned to investors.

The team once again highlight elevated, increasingly unattractive valuation levels in the market suggesting that these present "great sale opportunities but offer fewer investment ideas". As a result of this, the team re-iterated a desire to invest overseas and/or build cash in the portfolio.

Key considerations/developments
Schroders is a publicly listed asset management company, which is still controlled by the family; the **client base** is fairly stable and the **investment process** has not changed. The UK Value product, in which Falkirk is invested, runs approximately £4.6bn in assets split roughly 1/3rd institutional and 2/3rd retail. The **investment team** appears to be stable and demonstrates

high conviction in its investment approach. UK & European equity teams have merged though there will be limited impact on the UK Value team.

Schroders Property Multi-Manager

(7.1% of Total Fund)

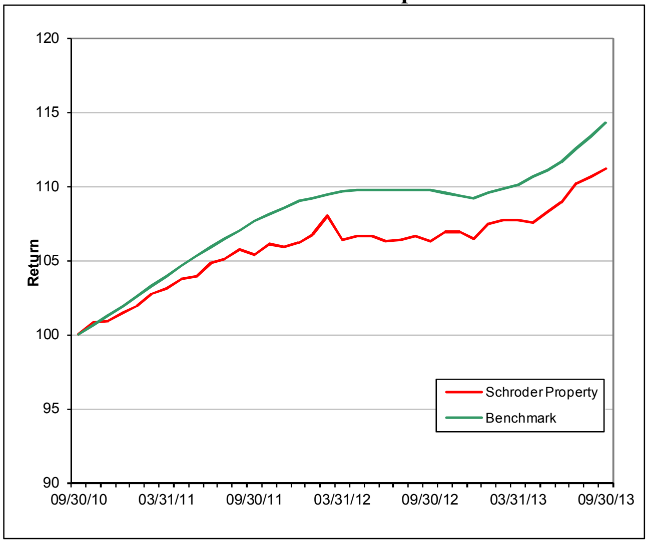
Investment Approach:

Schroders runs a segregated mandate providing a multi-manager portfolio of property funds. The manager seeks to identify attractive property markets and property funds with skilled managers, some of which are sector specialists.

Investment Objective:

To outperform IPD UK Pooled / Quarterly Property All Balanced Funds Weighted Average Index by 0.75% per annum (net of fees) over 3 year rolling periods (inception date April 2006)

3 Year Performance to 30 September 2013



Q3 2013	: -0.3% excess return
3 Year	: -1.0% p.a. excess return
Since inception	: +0.2% p.a. excess return

Summary

Latest 3 year performance remains weak (-1.0%pa relative). Since inception, the performance is broadly in line with the benchmark, but less than the objective. Significant restructuring undergone to position the portfolio for the future

Portfolio

The portfolio is comprised of a diverse group of funds investing in property assets largely in the UK. Continental European exposure amounts to approximately 8% of the portfolio.

The poor three year relative performance has been dominated by exposure to Continental Europe, which is not included in the benchmark – 10% of the portfolio was committed to Europe in 2006/07. Returns from European property continued to lag UK property performance in the third quarter. In addition, transaction costs and cash drag in a rising market affected performance.

The portfolio is valued at £105m. £15m of new equity was added between Dec '09 and Jun '10. Activity has been fairly significant – since Q1 2009, >£80m of property transactions have taken place, replacing 6 holdings with 6 new funds (inc L&G Managed Property Fund during Q2 '13). The impact of changes is to shift the portfolio closer to the benchmark, which may make it more difficult to achieve the outperformance objective, but makes it more likely that benchmark-like returns are achieved in future.

The portfolio's risk profile has been rebalanced through greater investment in low geared, balanced property funds and those funds targeting an income focussed approach. As a result, the manager believes the portfolio is well positioned for the current investment environment, in which the income yield on property is very competitive with government bonds.

Cash has fallen from more than 15% in 2009 and represents 0.6% at end September 2013.

Key considerations/developments

Schroders is a publicly listed asset management company, which is still controlled by the family; the **client base** is fairly stable and the **investment process** has not changed. The **investment team** appears to be stable, but the poor performance puts it on the defensive.

APPENDIX 3 – GLOSSARY

Benchmark - The yardstick used to measure the success and structure of a portfolio. All managers are measured against benchmarks. Passive managers are tasked with producing returns that are the same as the benchmark. Active managers are tasked with producing returns that are higher than the benchmark.

Benchmark return - Identifies the total return of the benchmark for the identified period. Return numbers for periods of one year or less show the actual return over the period. Returns for periods of greater than one year are annualised returns - they show the return per annum (%pa).

Dividend Yield - The dividend a company pays divided by its current price.

Duration - A measure of the sensitivity to interest rates of bonds. It identifies the approximate percentage change in a bond's price for a 100 basis point change in yield

Excess Return - Is the out / underperformance of the portfolio relative to the benchmark for the identified period. Return numbers for periods of one year or less show the actual return over the period. Returns for periods of greater than one year are annualised returns - they show the return per annum (%pa).

Investment Objective – All managers (and the Fund) are set investment objectives, which are related to a specific benchmark. The investment objective for a passive manager is to match the returns of the benchmark. The investment objective for an active manager is to exceed the returns of the benchmark by a pre-determined percentage per annum over a pre-determined period.

Market value (£) - Identifies the total market value of the portfolio / Fund

Portfolio return - Identifies the total time weighted rate of return of the assets of the portfolio for the identified period. Returns for periods up to 12 months are the return over that period. Returns for periods longer than 12 months are annualised returns – they show the return per annum (%pa).

Turnover - Is the level of purchases and sales for the period. High turnover is generally regarded as bad because trading costs are incurred.