AGENDA ITEM 6

FALKIRK COUNCIL

Subject: **FUND MANAGER PERFORMANCE REVIEW**
Meeting: **PENSIONS COMMITTEE AND PENSION BOARD**
Date: **10 DECEMBER 2015**
Author: **DIRECTOR OF CORPORATE AND HOUSING SERVICES**

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 reviews individual manager performance and developments.

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.

- Aberdeen Asset Management (AAM) – MSCI All Countries World Index
- Baillie Gifford Bonds (BGB) – a customised benchmark comprising UK Fixed Interest and UK Index Linked Bonds
- Baillie Gifford Diversified Growth (BGDG) – UK base rate
- Legal & General (L&G) – a customised benchmark comprising UK and Overseas Equities
- Newton Investment Management (NIM) – the MSCI AC World (NDR) Index
- Schroder Investment Management (SIM)
    - (i) UK Equities – the FTSE All Share Index
    - (ii) 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 During the third quarter, equity markets were weak due to speculation that the US Federal Reserve might raise interest rates and due to concerns over the health of the Chinese economy. European & US equity markets declined by around 8-10%, Japanese equities fell 15% while the Chinese stock market fell 24%.

2.2 The US central bank appeared to be close to raising rates in August. However, this coincided with the release of very weak Chinese economic data, and a sell-off in global equity markets, which ruled out an immediate rate rise.

2.3 Bond markets performed well (prices rose and yields fell) during the quarter, benefiting from a further decline in the oil price and flight to quality flows from equities. UK, US & German 10 year bond yields fell by 0.2%-0.3%. The best performing bond markets were Italy & Spain, where yields fell 0.4% - 0.6%. Peripheral European bond markets benefited from greater confidence that Greece would not default or leave the EMU.

2.4 Oil price weakness was another feature of the third quarter. The oil price fell 25%, largely due to the Chinese economic slowdown. The oil price has fallen to a 10 year low and has fallen over 60% from its 2013 peak.

2.5 The outlook for global equity and bond markets critically depends on US monetary policy. The markets already expect a 0.25% increase in interest rates in the fourth quarter and two more 0.25% increases during 2016. If this gradual pace of tightening occurs, the recovery in the global economy should not be derailed and equity and bond markets should react benignly. In terms of currencies, higher US interest rates should benefit the US dollar, especially against the Euro as the European central bank's monetary policy shows no signs of tightening.

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 2015 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 Global equity market indices returned -5.4% in sterling terms over the third quarter of 2015. Returns were positively influenced by the weakness of sterling (-4% to -6%) against the Euro, Dollar and Yen. The FTSE All Stock gilt index rose 3.1% and the FTSE Index Linked gilt index returned +1.9%. The Fund's UK commercial property benchmark index rose +3.1%.

3.3 The overall Fund's return of -3.2% over the quarter was behind the benchmark return by -0.2%. Over the 3 year period the Fund benefited from equity and property market strength, NIM's outperformance in global equities, SIM's outperformance in UK equities and Baillie Gifford's outperformance of its Diversified Growth Fund cash benchmark. The Fund rose +8.9% per annum compared with the benchmark return of +7.5% per annum, an excess return of +1.4% per annum. Long term return data shows Fund appreciation of +8.1% per annum over 5 years and +6.9% per annum since September 2001. These long term returns are above the benchmark returns.

3.4 Over the third quarter of 2015, the returns of the Fund's three active equity managers ranged from -2.3% to -8.8%. AAM and SIM underperformed their respective benchmarks, while NIM outperformed. The Fund's passive equity manager, L&G, produced a return of -5.8%, in line with its benchmark return, and so consistent with its mandate.

The return from BG's bond mandate was +2.4%, ahead of its benchmark by +0.5%. BG's other mandate, the Diversified Growth portfolio, fell -2.6%, behind its benchmark by -2.8%.

The property portfolio managed by SIM rose +3.1%, in line with its benchmark.

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 above the benchmark over 5 year rolling periods. Returns over the past 5 years and since inception have beaten the benchmark comfortably, but they have not achieved the objective.

The AAM mandate's objective is +3% per annum outperformance over 3 year rolling periods. Performance is lagging the benchmark and the objective by a wide margin over 3 years and since inception.

The performance of BG's bond mandate is essentially in line with its benchmark since inception in 2007, but the 3 and 5 year performance have been strong, ahead of the benchmark and in line with the objective. The excess return over the benchmark of +0.8% per annum is close to 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 broadly in line with its benchmark, but has fallen short of the objective by 0.9% per annum.

4. CONCLUSION

4.1 The third quarter of 2015 was characterised by sharp falls in equity markets occasioned by a faltering Chinese economy, uncertainty surrounding interest rate rises in the US and the continuing slump in oil prices. By contrast, bonds had a positive quarter as investors sought a safe haven away from equities. The deterioration in global economies saw the Bank of England hold UK interest rates at 0.5%.

4.2 Overall, the fund narrowly missed its benchmark. Newton Global Equities and Baillie Gifford Bonds were both strong performers in the face of market turbulence. However, Schroders UK Equities and Baillie Gifford Diversified Growth were both below benchmark, albeit remaining solid performers over longer time periods. The performance of Aberdeen both in Q3 and cumulatively continues to give cause for concern and will clearly be a matter of discussion at this meeting and at the forthcoming investment sub group meeting.

5. RECOMMENDATIONS

5.1 The Committee and Board are asked to note:-

(i) the Managers' performance for the period ending 30 September, 2015, and

(ii) the actions taken by Managers during the quarter to 30 September, 2015 in accordance with their investment policies.

pp **Director of Corporate & Housing Services**
Date : 27 November 2015
Contact Officer: Bruce Miller, Alastair McGirr

LIST OF BACKGROUND PAPERS

1. The Northern Trust Company – Fund Analytics 30 September 2015

Any person wishing to inspect the background papers listed above should telephone 0131 469 3866 and ask for Bruce Miller

APPENDIX 1 – PERFORMANCE MEASUREMENT (RATES OF RETURN)

Rates of Return by Manager with Excess Returns - 30 September 2015							
			Returns				
Manager	**Market Value £**	**Weight**	**3 months**	**3 year**	**5 year**	**Since inception**	**Inception Date**
Aberdeen Portfolio	199,654,642	11.9%	-8.8%	3.6%	5.7%	5.4%	May-10
Benchmark			-5.9%	9.8%	8.2%	7.4%	
Excess Versus Benchmark			**-2.9%**	**-6.3%**	**-2.5%**	**-2.0%**	
Excess Versus Objective			-	**-9.3%**	**-5.5%**	**-5.0%**	
Baillie Gifford Bond Portfolio	152,913,133	9.1%	2.4%	6.3%	7.6%	6.6%	Mar-07
Benchmark			1.9%	5.5%	6.6%	6.7%	
Excess Versus Benchmark			**0.5%**	**0.8%**	**1.0%**	**-0.2%**	
Excess Versus Objective			**-**	**-0.1%**	**0.1%**	**-1.1%**	
Baillie Gifford Diversified Growth	199,334,732	11.8%	-2.6%	5.0%	**-**	5.5%	Feb-12
Benchmark			0.1%	0.5%	**-**	0.5%	
Excess Versus Benchmark			**-2.8%**	**4.5%**	**-**	**5.0%**	
Excess Versus Objective			**-**	**-**	**-**	**1.5%**	
Legal & General	342,018,648	20.3%	-5.8%	9.5%	8.1%	11.9%	Jan-09
Benchmark			-5.8%	9.4%	8.0%	11.8%	
Excess Versus Benchmark			**0.0%**	**0.1%**	**0.1%**	**0.1%**	
Excess Versus Objective			**0.0%**	**0.1%**	**0.1%**	**0.1%**	
Newton	259,714,793	15.4%	-2.3%	12.2%	10.3%	8.6%	Jun-06
Benchmark			-5.9%	10.0%	8.2%	6.9%	
Excess Versus Benchmark			**3.6%**	**2.3%**	**2.0%**	**1.7%**	
Excess Versus Objective			-	-	**-1.0%**	**-1.3%**	
Schroders UK Equity	219,037,490	13.0%	-7.6%	11.4%	9.3%	8.4%	Sep-01
Benchmark			-5.7%	7.2%	6.7%	6.2%	
Excess Versus Benchmark			**-1.9%**	**4.1%**	**2.6%**	**2.2%**	
Excess Versus Objective			-	**2.9%**	**1.3%**	**0.9%**	
Schroders Property	137,194,460	8.2%	3.1%	11.0%	7.8%	3.6%	Nov-05
Benchmark			3.1%	11.7%	8.9%	3.7%	
Excess Versus Benchmark			**0.0%**	**-0.7%**	**-1.1%**	**-0.1%**	
Excess Versus Objective			-	**-1.5%**	**-1.9%**	**-0.9%**	
Total Fund	1,682,709,373	100.0%	-3.2%	8.9%	8.1%	6.9%	Sep-01
Benchmark			-3.0%	7.5%	6.8%	6.6%	
Excess Return			**-0.2%**	**1.4%**	**1.4%**	**0.3%**	

*** Note that objectives vary and are set over 3 or 5 year periods highlighted in bold for each manager.**

There are small rounding effects in the table above.

APPENDIX 2 - INVESTMENT MANAGER COMMENTS

Aberdeen Global Equity

(11.9% of Total Fund)

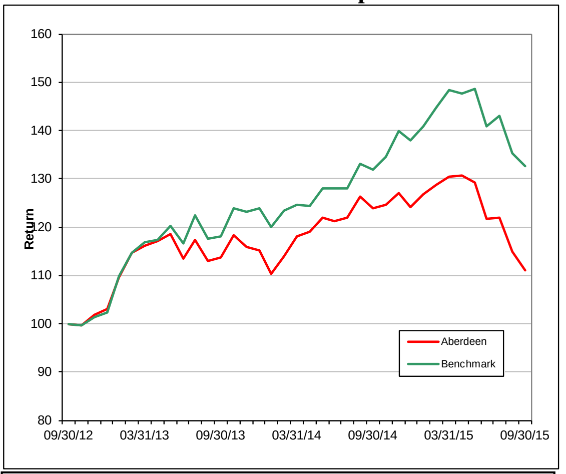
Investment Approach:

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)

3 Year Performance to 30 September 2015



Q3 2015	:	-2.9% excess return
3 Years	:	-6.3% excess return
Since inception	:	-2.0% p.a. excess return

Summary

Terrible 3 year and since inception performance – both below benchmark and objective. Significant asset outflows continue firm-wide. Rumours of firm being up for sale have been publicly denied.

Portfolio

A concentrated portfolio of 50 stocks should be able to achieve its objectives - it is largely unconstrained. 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 stands at 3.0%.

The generally defensive sector positioning is largely offset by a significant bias towards the collapsing energy and commodities segments. The portfolio remains u/w N. America by a very significant 20%. As the portfolio is not benchmark constrained this is not in itself a problem, but it is arguably the firm's natural bias towards Asia and emerging markets, which is driving this position rather than the lack of value that the team pronounce every quarter. Regional allocation has cost the portfolio over 3% and stock selection a further 7.5% in relative performance over 12 months. These are big numbers. By sector, the portfolio remains o/w consumer staples and has high relative exposure to materials and energy, although exposure to consumer discretionary remains low. The underrepresentation of financials has grown (-7%). The portfolio continues to perform poorly and, worryingly, its defensive tilt failed to protect it in the recent quarter when equity markets fell sharply. Aberdeen's process and sheer size mean that changes are mainly incremental. Activity increased as market falls meant more opportunities to top and tail existing positions. New buys: Checkpoint Software & M&T Bank. Sales: South32 & United Technologies.

In Q3, the portfolio lagged the index return by 2.9%, due to poor stock selection in the UK, Japan and North America as well as the o/w allocation to Brazil and u/w US stance. By sector, two-thirds of the underperformance was attributable to poor stock selection in financials (Banco Bradesco, Standard Chartered), with selection in industrials (Fanuc, Rolls Royce) and materials (Potash, Vale) also meaningful. The small drag from sector allocation was offset by the 3% cash position. The same themes explain the bulk of the 12 month underperformance, with poor stock selection and an o/w allocation in energy compounding the weakness.

Aberdeen continue to follow their process investing in good quality companies with lower than average levels of debt and relatively stable earnings/cash flows. They admit to mistakes (focussing too much on quality and not enough on valuation) and are looking at ways of "working smarter" [for example, by revisiting investment cases for disruptive technology stocks like Alphabet (Google)], without changing their philosophy or process – to which they remain unshakably committed. However, poor (and deteriorating) performance means there is a heightened risk of flows turning decisively negative, not least because consultants may well revisit Aberdeen's position on their 'buy' lists. We estimate that Aberdeen's Global strategies have already "lost" 30% of their performance-adjusted AuM over the last 2 years and arguably outflows are now driving (or at least exacerbating) the underperformance. Long term investors have remained loyal so far. Aberdeen has reduced the fee at Falkirk's request, but this is a small concession in the context of the performance.

Baillie Gifford Bonds
(9.1% of Total Fund)

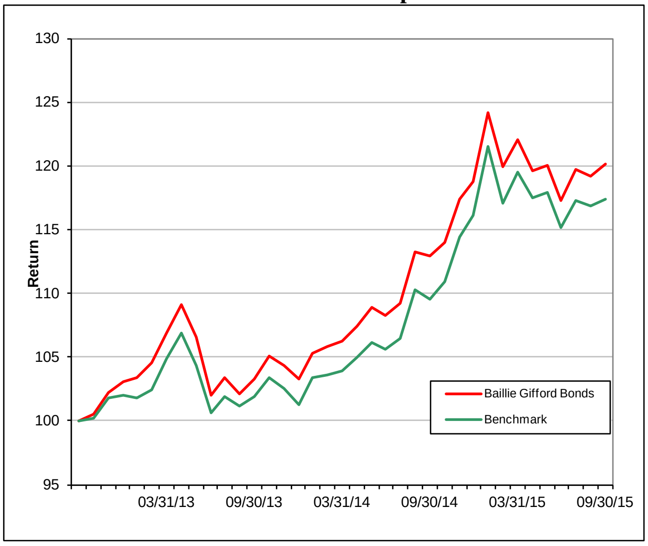
Investment Approach:

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 2015



Q3 2015	: + 0.5% excess return
3 Year	: +0.8% p.a. excess return
Since inception	: - 0.2% p.a. excess return

Summary

A strong Q3 takes 3 and 5 year performance close to objective before fees. Portfolio positioned for weaker credit environment. No major issues.

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.

Q3 was characterised by Chinese and emerging market economic weakness feeding through into lower commodity prices. This benefited government bonds with conventional gilts returning +3.1% (Q2: -3.4%) and index-linked gilts returning +2.3% (Q2 -3.3%). Investment grade bonds lagged, returning +1.0% (Q2: -3.9%) while high yield bonds returned -1.9% (Q2: -3.9%).

The portfolio outperformed by 0.5% in Q3. The main positive contributors to performance came from asset allocation in the corporate bond portfolio (+0.5%) and currency positioning (+0.4%). Negative contributors to performance came from some single names in the corporate bond portfolio (-0.4%) and stock selection in the index-linked portfolio (+0.2%).

Overall portfolio risk has declined slightly from 0.85% in Q2 to 0.78% in Q3. Emerging market currency exposure was reduced by closing a long Brazilian Real position. The portfolio is still structured to take advantage of a stronger US Dollar, largely against the Euro. The portfolio is also long of selected European peripheral currencies against selected South American currencies. The portfolio’s largest positions are 3% long US Dollar and 3% short Euro.

Portfolio duration is in line with the benchmark at 11.7 years. Asset allocation is underweight utilities and overweight securitised bonds. The credit quality of the portfolio (AA) is higher than that of the benchmark (A) as the manager is concerned about potential spread widening in the lower rated investment grade names.

Key considerations/developments

Baillie Gifford is a long established, reputable partnership; the client base is stable and the investment process has not changed.

Baillie Gifford Diversified Growth

(11.8% of Total Fund)

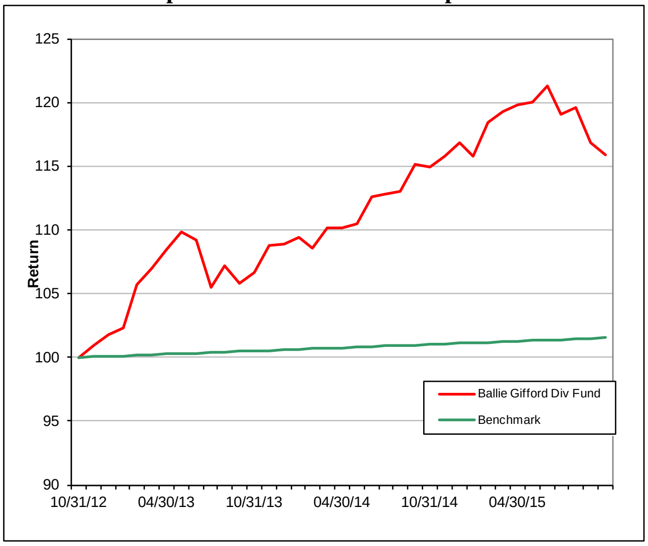
Investment Approach:

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 2015



Q3 2015	: -2.8% gross relative to base rate
3 Year	: +4.5% gross relative to 0.5% base rate
Since inception	: +5.0% gross relative to 0.5% base rate

Summary

Co-head of team (and ex Head of Risk at BG) moved to Aberdeen Jan 2015, which is a concern – the target return from here looks too high and estimated risk too low - notably BG claim that "Active Currency" contributes minus "-1.7%" to "predicted volatility". Capacity management concerns.

Portfolio

Q3 2015 loss essentially shows this fund delivers a return that is not enhanced cash, but watered-down equities, the portfolio's biggest asset and 60% of total risk. BG's September 2015 "long-term return expectations" report states that equities have the highest expected return at 3.75% pa over cash. Every other asset return is lower. With fees of 0.7% pa., none of the assets that they invest in will deliver the target return of cash plus 3.5% pa after fees. Unless they have the considerable skill to generate substantial outperformance, the stated target return is too high.

"Active Currency" risk is now stated at just "0.2% of assets" and "-1.7% of predicted volatility" (net). Yet Active Currency has consistently been one of the largest contributors to return over recent quarters. The net long currency positions are now 32% with similar net short making total net currency exposure around 65% of the fund – again by far the largest asset exposure. Q3 trading was £216m equity, £259m bonds and £14,540m currency forwards! It is unrealistic to think these huge currency bets have no risk (or negative risk!). The stated risk is too low.

The stated predicted volatility of the portfolio is now 7.1% net (14.2% before "Diversification effect") with 59.4% of this from equities. Targeted maximum volatility is 10%. (Global equities are 17.2%).

Key considerations/developments

Mike Brooks, co-head of team and ex- Head of Risk at BG, resigned in January, leaving the firm in March to join Aberdeen to launch a similar, but probably better designed, fund.

Baillie Gifford announced "closure" in the diversified growth strategy in Q4 2012 at £2.8bn, reflecting an estimated "capacity" limit of £5bn and "closure to all new clients" in June 2013. Yet, BG took on over £1bn of net inflows after this "closure" to reach £6bn. They have now launched a similar fund "to enable more capacity" (of "£10bn"), with "the same process run by the same people" (excluding c5% in Insurance-Linked Securities, which were a capacity constraint). Capacity management is a concern for this product and for the firm as a whole, but is not widely recognised.

Newton Global Thematic Equity

(15.4% of Total Fund)

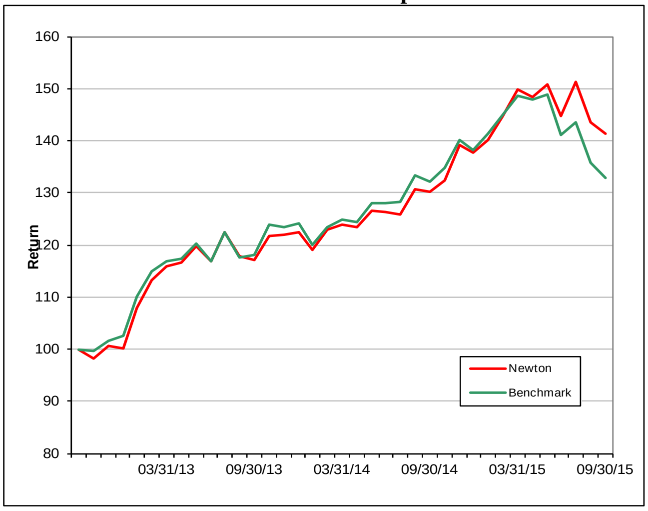
Investment Approach:

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 2015



Q3 2015	: +3.6% excess return (gross)
5 Years	: +2.0% p.a. excess return (gross)
Since inception	: +1.7% p.a. excess return (gross)

Summary

Another fantastic quarter, holding up well in falling market. Portfolio comfortably ahead of benchmark since inception, but still short of objective, especially net of fees. Active process taking advantage of changing valuations.

Portfolio

The portfolio is concentrated in just 44 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 very defensive stance and cash (mostly short term US Treasuries) was 6.8% at quarter end.

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

The portfolio remains overweight Europe/UK (+8%) equities and cash (+7%) and underweight Japan (-6%), Pacific (-5%) and Emerging Markets (-5%). The small underweight N. America has become a small overweight following a 5% investment in the region this quarter. There continues to be high relative exposure to companies in the consumer services sector (+8%), while financials (-13%), telecoms (-4%) and oil & gas (-4%) companies are significantly under-represented. The portfolio's high cash position and defensive tilt protected returns well during the recent equity market weakness even though there is less of a defensive tilt due to the greater representation of cyclical stocks in the portfolio than previously.

The portfolio beat its benchmark handsomely in Q3, due to positive relative returns from Europe and EM. There were positive relative contributions across all sectors apart from utilities and consumer services, in particular from oil & gas, technology and basic materials. The best individual stock contributions came from Google (renamed Alphabet), C.H. Robinson, RELX and TJX. Main detractors from performance included Trimble Navigation, TripAdvisor & Discovery Communications. Turnover and stock count rose as the portfolio took advantage of weakness to introduce several new stocks: Hershey, Merck, Wolseley, Emerson Electric, Mattel, Johnson Matthey and Stratasys. There were outright sales of L'Oreal, Kraft Heinz, Softbank and Vodafone. The cash/bonds position added significantly to relative performance (currency gain from US$).

Key considerations/developments

Newton remains one of Bank of New York Mellon's asset management subsidiaries based in London; the investment process is unchanged since a review in 2011/12 when personnel changes were made; the client base is stable (no flows in or out). Note – some recent stock purchases go against analyst recommendations.

Schroders UK Equity
(13.0% of Total Fund)

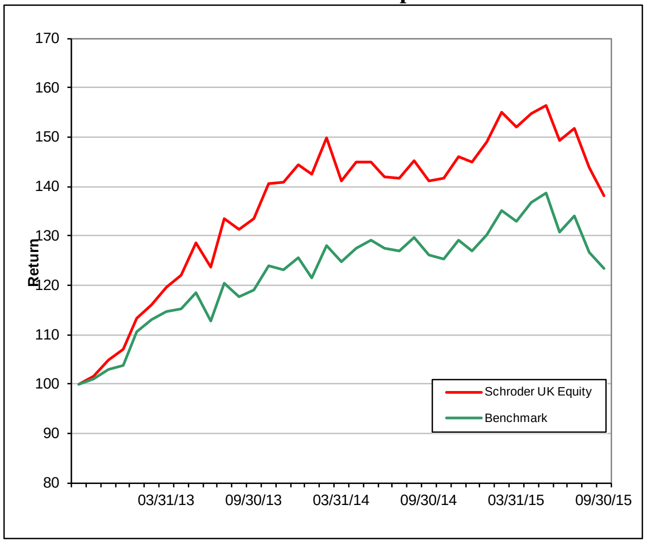
Investment Approach:

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 30 September 2001)

3 Year Performance to 30 September 2015



Q3 2015	: -1.9% excess return
3 Year	: +4.1% p.a. excess return
Since inception	: +2.2% p.a. excess return

Summary

The portfolio underperformed in Q3, but is comfortably ahead of benchmark and objective over 3 years. Clearly articulated strategy with stable ownership, client base and investment team.

Portfolio

The portfolio of 37 stocks deviates from the benchmark meaningfully, which means that the objective should be achievable, but the return profile is likely to be highly variable. Once again, active sector positions are very similar to last quarter. The portfolio retains an overweight position in the food & drug retailers and general retailers sectors. Tobacco & beverages are the largest underweight sectors and are both zero weighted.

The holding in Darty and the underweight Glencore were the biggest positive contributors to Q3 relative returns. Positions in Anglo American, Drax and Home Retail were the biggest detractors, alongside the underweight exposure to British American Tobacco and SABMiller.

The mining sector has been a greater focus of their attention over the last 6 months or so. While holding Anglo has detracted from returns, the team believe that the shares are undervalued reflecting Glencore's issues rather than Anglo's fundamentals. They remain comfortable with the balance sheet and asset backing, though would see sense in a short term dividend cut. Valuation is very attractive (lowest Price to Book ratio in 50 years). They have added to the position and also initiated a position in South32 within the sector, taking advantage of the current fear factor surrounding the materials names.

Amongst other metrics, the team focuses on cyclically adjusted P/E's when it comes to valuations. Banks and miners continue to look cheap on this basis with traditionally stable companies appearing expensive. The market continues its preference for stability up until now.

Andrew commented on some work currently being done on the global performance of value versus growth. The current period of value underperformance is incredibly extended in a historical context.

In terms of activity, they continue to take profits in names that have performed well such as Rentokil Initial and ICAP. The holding in Ladbrokes was sold following the recently agreed merger with Gala Coral.

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 investment process has not changed. UK Value product, in which Falkirk is invested, runs approximately £5.5bn in assets split roughly 1/3rd institutional and 2/3rd retail. Stable investment team, demonstrates conviction in its investment approach.

Schroders Property Multi-Manager
(8.2% of Total Fund)

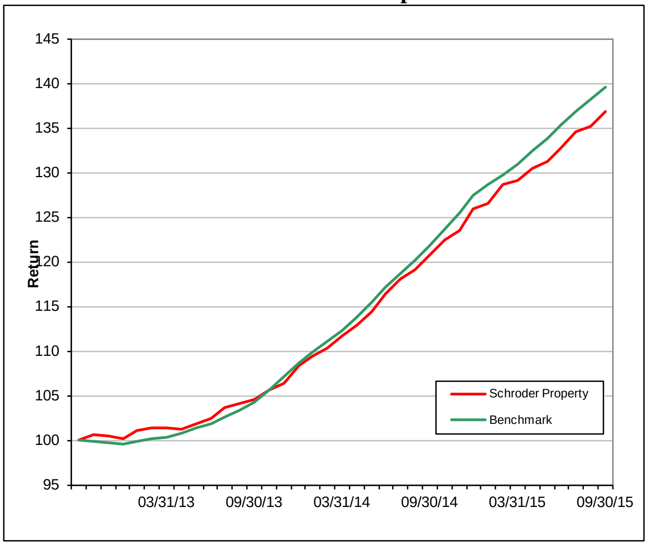
Investment Approach:

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 30 November 2005)

3 Year Performance to 30 September 2015



Q3 2015	:+0.0% excess return
3 Year	: -0.7% p.a. excess return
Since inception	: -0.1% p.a. excess return

Summary

Portfolio manager resigned, so resources under pressure; latest 3 year performance remains weak relative (-0.7% pa), but strong absolute (+11% pa). Portfolio has been restructured and is now positioned for the future.

Portfolio

The portfolio is comprised of a diverse group of 15 funds investing in property assets largely in the UK (93%). UK performance has outperformed the benchmark in each long/short period, but the Cont. European exposure remains a drag on performance except in Q3 when it returned 31.1% due to a large capital repayment. The portfolio is valued at £139m.

The manager has re-positioned away from London offices by continuously selling WELPUT[1] and has made commitments for investing in industrial property and a small lot size multi-sector partnership fund (Metro PUT via a new partnership managed by Hermes). The partnership fund is only available to Schroders' clients. No new purchase or sale has been made in this quarter, but Schroders is preparing to purchase a new fund - the Regional Office PUT to gain access to the rest of UK office market.

Continental Europe now amounts to 3% of the portfolio. (Recap in '06-07, 10% of the portfolio was committed to Europe.) The poor three year relative performance has been dominated by this exposure, which is not in the benchmark. Schroders is expecting the recovery in Europe will continue and plans to hold the exposure till maturity (2018).

The portfolio's risk profile has been rebalanced through greater investment in low geared, core 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.

Current cash level is 4% and uncommitted cash is 1.2%. Schroders' real estate return forecast is still 15% for 2015, but drops to 4% for next year and expects a small fall in capital value in either 2017 or 2018.

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** is changing meaningfully: last quarter, the fund manager departed and the portfolio analyst was promoted to be the fund manager. Fund manager access has been difficult during the transition period and the client relations manager has changed too. No quarterly update was arranged.

[1] West End of London Property Unit Trust

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.