AGENDA ITEM 11

FALKIRK COUNCIL

Subject:	**FUND MANAGER PERFORMANCE REVIEW**
Meeting:	**JOINT MEETING OF THE PENSIONS COMMITTEE AND PENSION BOARD**
Date:	**26 JUNE 2015**
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 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.

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 Bank of England 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	AREF/IPD UK Quarterly 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 A key feature of markets in the first quarter of 2015 was the strength of the US Dollar. With the dollar rising almost 5% against sterling, financial market returns in sterling terms were boosted as US assets represent a significant part of overseas holdings for most funds, including Falkirk's. A smaller part of the Fund is invested in Chinese equities, but the performance of the Shanghai Composite Index is worthy of note as it rose by 22% in Sterling terms – it has more than doubled over the last 9 months despite slowing economic growth as interest rates have been cut.

2.2 Over the course of 2015 global growth is expected to be approximately 3% in line with last year, but the momentum in forecasts continues to drift gently downwards. A weather-related weak first quarter in the USA, the world's largest economy (only 0.2% quarter on quarter growth) led to forecasts being cut from 3.5% to 2.5% for the full year.

2.3 On a positive note, equity investors were cheered by an unanticipated recovery in the Eurozone economies, and also by further monetary and fiscal easing in China, which should help to stabilise this heavyweight economy. The picture in Japan and most emerging markets is more mixed, and India is the only major developing country with a particularly positive economic outlook.

2.4 The deflationary scare that gripped asset markets during the final quarter of 2014 has somewhat dissipated as the Brent oil price rebounded from a low of around $46 per barrel in mid-January to its current level of $63. The turnaround in European economies (forecast growth of 1.5% in 2015) and the reversal of the deflationary sentiment caused an unsettling correction in European bond markets.

2.5 Consensus forecasts are for an increase in US interest rates later in 2015, although the timing continues to be pushed back. Unemployment has fallen from a peak of 10% to 5.5% since the global financial crisis. Growing wage pressure is expected to spur the Federal Reserve into action. Elsewhere in the world disinflationary pressures still predominate, so there is almost no prospect of tighter monetary policies in the immediate future except perhaps in the UK and struggling economies such as Brazil and Turkey.

2.6 US dollar strength against most world currencies peaked in April, but many investors believe that an increase in US interest rates could lead to renewed strengthening. Geopolitical risks such as the possible exit of Greece from the Eurozone, Chinese expansion in the South China Sea or a further deterioration in the Ukrainian situation would also be expected to favour the safe haven of the dollar.

2.7 Risks to the world economy and asset prices are to be found in the normalisation of US interest rate policy, poor liquidity in asset markets, and high and increasing debt levels. These uncertainties are unlikely to have an impact in the near future, and should be amenable to corrective policies if they do actually materialise.

2.8 Liquidity flows continue to dominate markets and investor sentiment, and the quest for yield continues. World stock markets are no longer cheap, but still offer superior opportunities to bond prices that have been boosted by expansionary conventional and unconventional monetary policies.

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 31 March 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 their 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 +7.5% in sterling terms over the first quarter of 2015. The FTSE All Stock gilt index rose 2.2% and the FTSE Index Linked gilt index returned 2.9%. The Fund's UK commercial property benchmark index rose +2.8%.

3.3 The overall Fund's return of +5.0% over the quarter was ahead of the benchmark return by 0.4%. Over the 3 year period the Fund benefited from equity market strength, Newton's (NIM) outperformance in global equities, Schroder's (SIM) outperformance in UK equities and Baillie Gifford's (BG) outperformance of the cash benchmark, rising +12.0% per annum compared with the benchmark return of +9.8% per annum, an excess return of +2.2% per annum. Long term return data shows Fund appreciation of +9.7% per annum over 5 years and +7.6% per annum since September 2001. These long term returns are above the benchmark returns.

3.4 Over the first quarter of 2015, the returns of the Fund's three active equity managers ranged from +4.9% to +8.7%. SIM and NIM outperformed their respective benchmarks, while Aberdeen (AAM) underperformed. The Fund's passive equity manager, Legal and General, produced a return of +7.0%, in line with its benchmark return, and so consistent with its mandate.

The return from BG's bond mandate was +2.7%, behind its benchmark by 0.3%. BG's other mandate, the Diversified Growth portfolio, rose 3.5%, ahead of its benchmark by 3.4%.

The property portfolio managed by SIM lagged its benchmark by 0.3%, but rose 2.5% 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 above the benchmark over 5 year rolling periods. Returns over the past 5 years and since inception have beaten the benchmark, but they have not quite achieved the objective.

The AAM mandate 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, albeit the manager retains the strong endorsement of the investment adviser.

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 very strong. The excess return over the benchmark of +1.2% 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 in line with its benchmark, but has fallen short of the objective by 0.7% per annum.

4. CONCLUSION

4.1 The quarter experienced two key developments which had a soothing effect on markets, namely a stabilising of oil prices and an unexpectedly ambitious bond buying initiative from the ECB. Improving levels of job creation and falling unemployment have led to a sharp strengthening in the US dollar and an increased likelihood in US interest rate rises.

4.2 The Fund achieved a return of 5% during the quarter outperforming its benchmark by 0.4%. This was led by a strong performance from Newton and solid performances from Schroder UK Equities and Baillie Gifford's Diversified Growth Fund. Schroder Property and Baillie Gifford Bonds fell just short of achieving the quarterly benchmark. However, Aberdeen's performance was again well below benchmark, albeit that, for the moment they retain the confidence and endorsement of Hymans Robertson, the Fund's investment adviser. In the circumstances, Aberdeen have been asked to present to the joint meeting of Committee and Board on 26 June.

5. RECOMMENDATIONS

5.1 The Committee is asked to note:-

(i) the Managers' performance for the period ending 31 March, 2015; and

(ii) the action taken by Managers during the quarter to 31 March, 2015 in accordance with their investment policies.

Chief Finance Officer

Date: 10 June 2015

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

1. The Northern Trust Company – Fund Analytics 31 March 2015

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 - 31 March 2015

Manager	Market Value £	Weight	Returns 3 months	3 year	5 year	Since inception	Inception Date
Aberdeen Portfolio	234,460,332	13.2%	5.2%	9.8%	-	9.6%	May-10
Benchmark			7.6%	14.1%	-	10.7%	
Excess Versus Benchmark			**-2.4%**	**-4.3%**	**-**	**-1.2%**	
Excess Versus Objective			**-**	-7.3%	**-**	-4.2%	
Baillie Gifford Bond Portfolio	155,361,175	8.7%	2.7%	9.0%	9.6%	7.2%	Mar-07
Benchmark			3.0%	7.8%	8.4%	7.4%	
Excess Versus Benchmark			**-0.3%**	**1.2%**	**1.1%**	**-0.2%**	
Excess Versus Objective				**0.3%**	**0.2%**	**-1.1%**	
Baillie Gifford Diversified Growth	206,044,737	11.6%	3.5%	7.2%	-	7.5%	Feb-12
Benchmark			0.1%	0.5%	-	0.5%	
Excess Versus Benchmark			**3.4%**	**6.7%**	**-**	**7.0%**	
Excess Versus Objective *			**-**	**-**	**-**	3.5%	
Legal & General	377,582,240	21.2%	7.0%	13.4%	9.8%	14.7%	Jan-09
Benchmark			7.0%	13.3%	9.7%	14.6%	
Excess Versus Benchmark			**0.0%**	**0.1%**	**0.1%**	**0.1%**	
Excess Versus Objective			**-**	**0.1%**	**0.1%**	**0.1%**	
Newton	275,315,700	15.5%	8.7%	16.1%	11.8%	9.8%	Jun-06
Benchmark			7.7%	14.2%	10.0%	8.7%	
Excess Versus Benchmark			**1.1%**	**1.9%**	**1.8%**	**1.1%**	
Excess Versus Objective			**-**	**-**	**-1.2%**	**-1.9%**	
Schroders UK Equity	241,109,512	13.5%	4.9%	16.6%	11.5%	9.5%	Sep-01
Benchmark			4.7%	10.6%	8.3%	7.1%	
Excess Versus Benchmark			**0.3%**	**6.0%**	**3.2%**	**2.5%**	
Excess Versus Objective			**-**	**4.8%**	**1.9%**	**1.2%**	
Schroders Property	129,433,476	7.3%	2.5%	8.9%	7.3%	3.1%	Nov-05
Benchmark			2.8%	9.4%	8.5%	3.2%	
Excess Versus Benchmark			**-0.3%**	**-0.6%**	**-1.2%**	**-0.1%**	
Excess Versus Objective			**-**	**-1.3%**	**-2.0%**	**-0.8%**	
Total Fund	1,780,639,246	100.0%	5.0%	12.0%	9.7%	7.6%	Sep-01
Benchmark			4.6%	9.8%	7.9%	7.2%	
Excess Return			**0.4%**	**2.2%**	**1.8%**	**0.4%**	

*** Note that objectives are set over 3 or 5 year periods.**

There are small rounding effects in the table above.

APPENDIX 2 - INVESTMENT MANAGER COMMENTS

Aberdeen Global Equity

(13.2% of Total Fund)

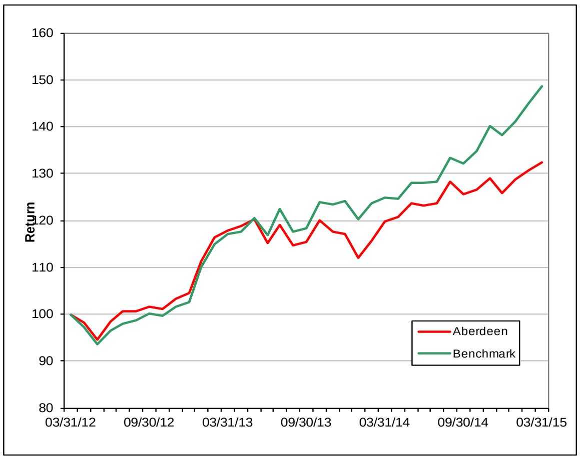
Investment Approach:

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 31 March 2015



Q1 2015	:	-2.4% excess return
3 Years	:	-4.3% excess return
Since inception	:	-1.2% p.a. excess return

Summary

Poor 3 year performance continues and outflows of ~30% in last 2 years could be exacerbating the situation. Since inception performance is now deteriorating too.

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 currently at 3.2%.

Sector and country positioning remains defensive and stable. N. America represents 55% of the benchmark, but the portfolio is u/w by 18%. The fund is o/w the UK (+8%), Europe ex-UK (+4%, with Switzerland +8%), and LatAm (+5%). By sector, the portfolio remains o/w consumer staples (+8%), and has high relative exposure to energy (+3.5%). The exposure to cyclical earnings has increased, with materials and industrials now overweight (in contrast to 2 years ago), although exposure to consumer discretionary remains low. The underrepresentation of financials has grown. The portfolio continues to perform poorly in strong equity markets, but its defensive tilt should help protect it in the event of equity markets falling. Aberdeen's views remain ever cautious, especially on US market valuations although the US weight is the highest in several years following 2 new US buys in the quarter (TJX & Cognizant). There was also 1 new UK buy (Experian).

In Q1, the portfolio managed to return a healthy 5.2%, but this lagged the index return by a meaningful 2.4%, due to overweight position in Brazil (which fell 10%), and poor stock selection in both Brazil and the US. By sector, the underperformance was attributable to poor stock selection in materials, healthcare and consumer discretionary sectors, offset by positive selection in industrials. There was also a drag from the underweight position in consumer discretionary stocks, which performed well. Positive stock contributions came from Fanuc (which rose 39%), Atlas Copco and CVS Health, but these were overshadowed by disappointments from Brazilian stocks Vale (which fell 30%) and Banco Bradesco, as well as Royal Dutch Shell, Potash Corp and Philip Morris.

Aberdeen continue to follow their process investing in good quality companies with lower than average levels of debt and relatively stable earnings/cash flows. However, poor 3 year 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" 29% of their performance-adjusted AuM over the last 2 years and arguably outflows are now driving (or at least exacerbating) the underperformance. Portfolio activity picked up, with 3 new stocks this quarter (see above), funded from sales in ENI and Centrica, and reductions in various staples.

Key considerations/developments

Ownership has not changed; the **client base** looks stable due to segregated fund client inertia yet AuM has declined ~30% over last 2 years as pooled fund assets steadily withdrawn (£2.3bn lost in Q1); the **investment process** has not changed/is standardised across equity products although relies on country/regional team picks for opportunity set. Cross-fertilisation of ideas and team-led approach key selling points. Stable, well-resourced and experienced **investment team** (6 most senior team members average >19 years in industry and >12 years at Aberdeen), backed up by extensive and experienced regional teams.

Baillie Gifford Bonds

(8.7% of Total Fund)

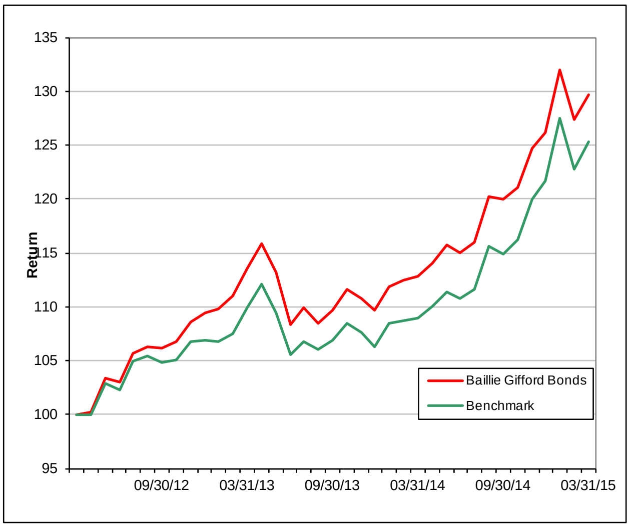
Investment Approach:

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 31 March 2015



Q1 2015	: - 0.2% excess return
3 Year	: + 1.2% p.a. excess return
Since inception	: - 0.2% p.a. excess return

Summary

Despite weakness in recent quarters, still a good 3 and 5 year performance, ahead of the objective by 0.3% pa and 0.2% pa respectively.

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.

Although the exceptional returns of Q4 2014 could not be repeated, bonds still had yet another good quarter. With UK inflation reaching zero and the search for yield at virtually any price continuing, Corporate Bonds returned 3.3% over the quarter as the spread to Government bonds, which returned 2.2%, narrowed. Index Linked Gilts also returned 3.3%.

In relative terms, the portfolio underperformed slightly returning 2.7% compared with 3.0% for the benchmark. Currency was a marginal positive, a significant turnaround from the previous quarter’s -1.1% contribution. Although the manager had expressed conviction in overweight positions in Mexico and Colombia, the latter position was closed off along with the Norwegian exposure due to the effect of the falling oil price. The portfolio’s largest positions are now 5.8% long US Dollar and 2.4% long Mexican Peso offset by a 3.1% short position in the Euro and 2.0% in the Thai Baht.

Last quarter, the Rates and Currency Team were reassessing the weight it placed on political considerations. This has resulted in strengthened global macro factors in the country model, but has not resulted in any significant change to the current portfolio positioning.

The two largest Brazilian bonds, Votorantim Cimentos and Odebrecht, were the worst performers over both a 3 and 12 month period. Both have now been sold. The longer dated Brazilian Index Linked Bond holding was also reduced. The manager no longer holds any positions in Emerging Market Credit – risk in this category is not priced appropriately. More generally, Credit is considered to be about fair value.

The tracking error increased from 0.79% to 0.88%, with Stock Selection now accounting for 58% of the risk relative to the benchmark (Q4: 47%). Currency has reduced from 32% to 20% of the portfolio risk.

Key considerations/developments

Baillie Gifford is a long established, reputable partnership; the client base is stable and the investment process has not changed. Assets under management in the sterling aggregate product decreased from £732m to £684m over the quarter. The manager had previously intimated the loss of two clients (£60m) from the Fund, one a small client transitioning to an LDI approach, and the other simply reducing their Bond exposure.

Baillie Gifford Diversified Growth

(11.6% of Total Fund)

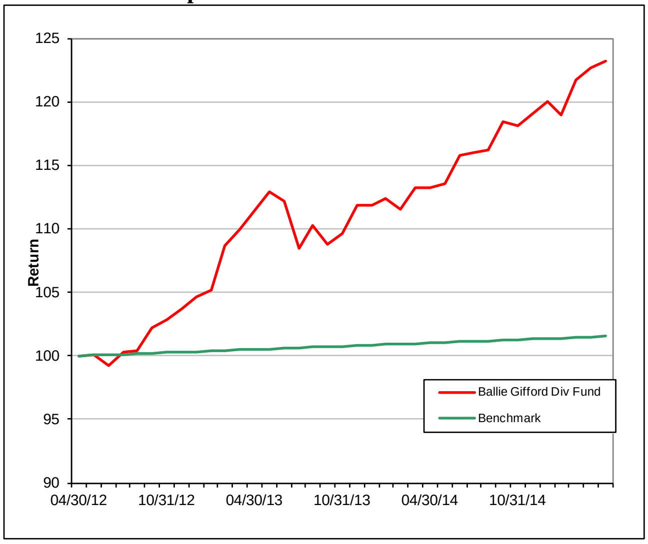
Investment Approach:

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 31 March 2015



Q1 2015	: +3.4% relative to base rate
1 Year	: +8.3% relative to base rate
Since inception	: +7.0% relative to base rate

Summary

Co-head of team resigned Jan 2015. As ex Head of Risk at BG, this is a concern as the target return from here may be too high and estimated risk may be too low - notably "Active Currency" at minus "-1.7% of predicted volatility".

Portfolio

"Active Currency" risk is now stated at "-0.3% of assets" and "-1.7% of predicted volatility" - very low given that it was the second biggest contributor to return in Q1, and in Q4 and Q3 it was by far the largest contributor to return. The net long and short FX positions are both around 40% of the fund, so total FX exposure is around 80% of the fund – again by far the largest asset exposure. Q1 trading was £309m equity, £561m bonds and £14,618m FX forwards. The stated risk underestimates possible FX losses/gains.

Insurance Linked bonds are 5.2% of the fund but are quoted at "0.4" of the risk. This also seems an extraordinarily low figure for what is essentially writing "catastrophe" insurance. The manager claims not to have major exposure to any one catastrophe risk.

Net performance has beaten the modest cash + 3.5% pa target since inception, but the manager forecasts "lower returns than in recent years": no asset class is forecast to achieve cash +3.5% pa net.

The stated predicted volatility is now 6.3% - with 61% of this from (listed and private) equities, which are 23% of fund. Targeted maximum volatility is 10%. (Global equities are 17.1%).

Key considerations/developments

Mike Brooks – co-head of team – resigned 21st January and left the firm in March. But there is no stated intention to change the process. There are 3 remaining members of the team and they are "having a chat" with potential replacements, but apparently in no hurry to make additions.

With 5.9% invested in the "Baillie Gifford Global Alpha" fund, the changes here might be a concern: Charlie Plowden leaves on a 3 month sabbatical just as this team integrates c£1bn of Monks' AuM.

After 0.7% charges, none of the manager's 10-year expected returns on any asset class now meet the net fund performance target of cash plus 3.5% net.

Baillie Gifford announced £5bn "capacity" in the strategy in Q4 2012, and "closure to all new clients" in June 2013. In Q1 2015 clients fell by 4 to 239. But on £40m more net inflows, assets increased to £5.96bn - £992m net inflows since this "closure".

Newton Global Thematic Equity

(15.5% of Total Fund)

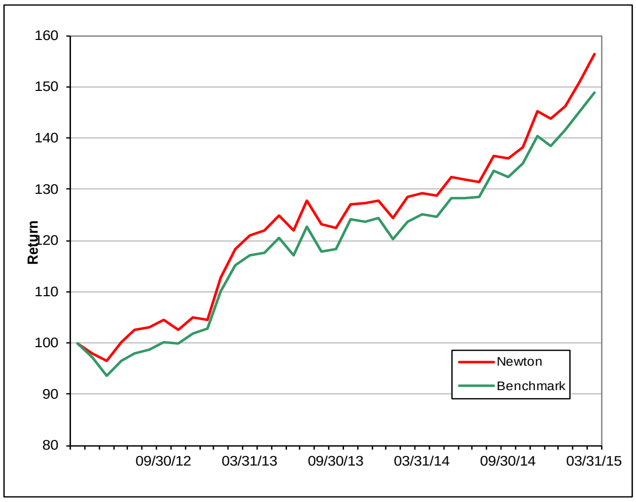
Investment Approach:

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 31 March 2015



Q1 2015	: +1.1% excess return
5 Years	: +1.8% p.a. excess return
Since inception	: +1.1% p.a. excess return

Summary

Portfolio is ahead of benchmark since inception, but is well short of meeting objective, especially net of fees. It is creditable that the portfolio has beaten the index return over the 5 year bull market as it has been constructed to take advantage of weak equity markets.

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 9.4% 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.

Little change to geographic or sector positioning. The portfolio remains overweight Europe/UK (+9%) equities and cash (+9%), and underweight all other regions. It continues to have high exposure to companies in the consumer services sector, while financials and oil & gas companies are still significantly under-represented. The portfolio is 6% overweight industrials compared to a 6% underweight a year ago while the consumer goods sector exposure has been sharply cut in favour of consumer services. Oil and gas and basic materials weights have also been cut over the last year. The portfolio's high cash position should continue to protect it if equity markets fall, but there is less of a defensive tilt due to the underrepresentation of cyclical stocks in the portfolio than previously.

The portfolio beat its benchmark again in Q1, mainly due to excellent stock selection in the US. The portfolio's underweight exposure to Oil & Gas was again a key benefit, while stock selection in financials (Equifax, AIA), consumer goods (Kraft, Japan Tobacco) and consumer services (Walgreen Alliance Boots) was positive. Stock selection in industrials (Trimble Navigation) and telecoms detracted from relative performance, as did the high cash/bond position (mitigated somewhat by the FX gain from holding US Treasuries). During the quarter, TripAdvisor and Vivendi were added to the portfolio; Yamana Gold, Continental and GlaxoSmithKline were sold outright.

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).

Schroders UK Equity

(13.5% of Total Fund)

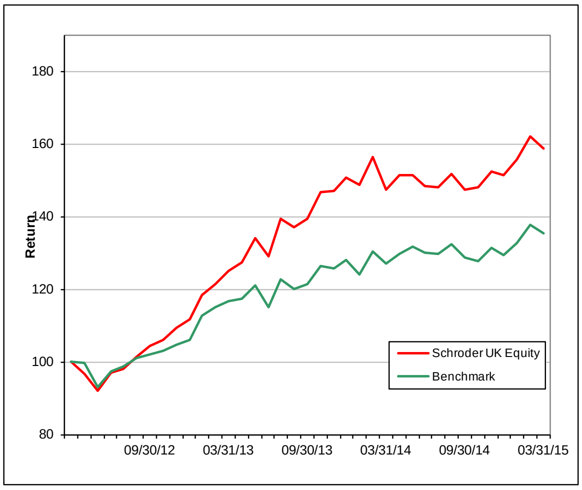
Investment Approach:

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 31 March 2015



Q1 2015	: +0.3% excess return
3 Year	: +6.0% p.a. excess return
Since inception	: +2.5% p.a. excess return

Summary

Modest outperformance in Q1. The manager is comfortably ahead of the objective over 3 years. Clearly articulated strategy with stable ownership, client base and investment team.

Portfolio

The portfolio of 38 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 very similar to last quarter. The portfolio retains an overweight position in the food & drug retailers and life insurance sectors, while mining is the biggest underweight.

Tesco, Friends Life and ICAP were the biggest positive contributors to relative returns in the quarter while positions in Royal Bank Of Scotland and Home Retail were the biggest detractors.

The message from the manager is a consistent one. With the market at an all time high, they find it difficult to find new opportunities with the appropriate risk and reward characteristics. As such, cash remains elevated at ~6.7% of the portfolio (~7% if we include cash within the Recovery Fund). The team stress the importance of sticking to the process and are confident that the value discipline will result in outperformance of the broader market.

A significant proportion of the quarterly report is dedicated to the idea that consistent long term results require a disciplined, repeatable process, while short term outcomes are driven by luck. With cyclically adjusted P/E's (CAPE) somewhat above long term averages, this suggests "reasonable" returns on a 10 year view. It would seem that a 7% cash position is a short term call on the market rather than a focus on the long term discipline.

A significant proportion of the team's time was spent looking more closely at the basic materials sector. While it screens as undervalued looking at 10 year CAPE, the team prefer to use an extended period of 20 years for this sector. Schroders added to Anglo American in the quarter but feel Rio & BHP are not currently attractive enough. A new position was initiated in Drax (UK coal-fired power generator) where a number of headwinds have pressured the share price and the team see long term value. Profits were taken in retailer Dixons Carphone which has performed very well in recent years.

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 £5.8bn in assets split roughly 1/3rd institutional and 2/3rd retail. Stable investment team, demonstrates conviction in its investment approach. Cautious on UK valuations.

Schroders Property Multi-Manager
(7.3% of Total Fund)

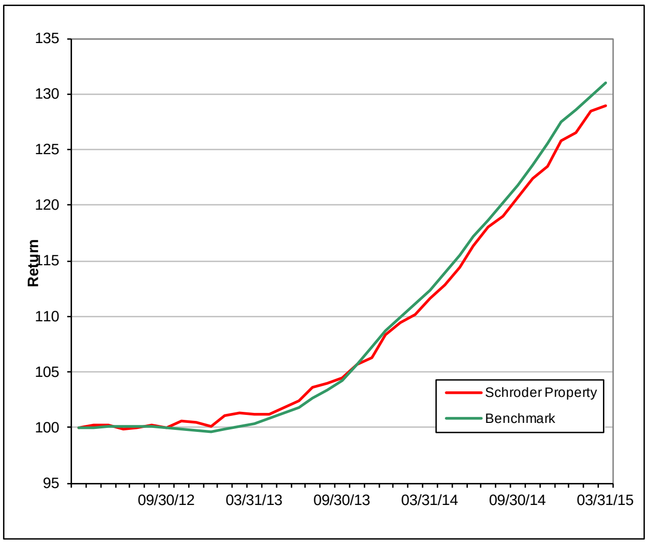
Investment Approach:

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 31 March 2015



Q1 2015	: -0.3% excess return
3 Year	: -0.6% p.a. excess return
Since inception	: -0.1% p.a. excess return

Summary

Latest 3 year performance remains weak relative (-0.6% pa), but strong absolute (+8.9% pa). In line with the benchmark since inception, but less than the objective. 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 (96%). The portfolio is valued at £130.5m. High transactional activities have impacted the short term performance.

The manager has re-positioned away from London offices and has made commitments for investing in industrial property (via a new partnership managed by a specialist at Jones Lang), which will utilise cash holdings.

Continental Europe now amounts to 4% of the portfolio. It finally produced a positive return due to asset disposals, but the positive return was offset by EUR/GBP depreciation. (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 exposures 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.

Given a constructive outlook, the manager targets to hold minimal amounts of cash, which will be 0.2% after the above commitments have been drawn (2.2% as of 31/03/2015).

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 has put it on the defensive.

Schroders' real estate return forecast for the next 3 years is 15%, 7.5% and 0%.

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.