

Summary report

Introduction

Due to the time lag between the end of the quarter and the availability of full performance data and explanation, the Officers have requested an interim report to help inform the Pensions Board. This report is intended to supplement and update the formal quarterly IMR report on the performance of the Fund at the aggregate level and to provide timely comment on the Fund's managers.

The first section provides a short review of economic and market conditions in recent months. The second section comments on the Fund's investment managers and highlights any business updates. The third section provides updated manager valuations and performance (where available).

Market returns

UK	31 Mar 15 - 28 May 15*	To 31 May 15 3 mths	To 31 May 15 12 mths
EQUITIES	5.2	4.7	6.6
BONDS			
Conventional gilts	-2.0	2.2	13.9
Index-linked gilts	-1.2	2.9	18.6
Credit	-1.7	3.2	13.1
PROPERTY	1.0	3.0	19.5
STERLING			
v US dollar	3.0	-4.8	-11.0
v euro	1.3	7.3	14.3
v Japanese yen	6.7	-4.8	3.7

Global	31 Mar 15 - 28 May 15*	To 31 March 15 3 mths	To 31 March 15 12 mths
EQUITIES	3.4	5.0	19.2
North America	2.8	1.3	25.1
Europe ex UK	2.2	15.3	7.7
Japan	8.6	10.8	27.1
Dev. Asia ex Jap	0.7	7.1	10.6
Emerging markets	4.8	5.0	16.3
GOV'T BONDS	-1.6	2.1	8.1
HEDGE FUNDS	0.0	2.5	0.0
COMMODITIES	3.5	-5.9	-20.4

Total return in local currency (\$ for Hedge Funds and Commodities)
 *Property and Hedge Funds to end April 2015

Q2 15 Market Update to end May

- The pace of global economic activity has remained subdued, with little rebound in the US and further slowdown in China. The modest recovery in the Eurozone does seem to be intact.
- Annual UK CPI inflation fell below zero in April but recovered again in May. The Bank of England still expects it to climb slowly to the 2% target as the influence of temporary factors – lower energy and food prices, sterling strength – wanes.
- US interest rates are still expected to rise later in the year.
- 10-year German government bond yields fell below 0.1% p.a. in the middle of April, but then rose sharply and settled around year-end levels by the end of May. Equivalent US and UK government bond yields have also risen back to year-end levels in recent weeks.
- Currency markets have broken out of recent trends. In trade-weighted terms, the euro has risen a little from its lows of mid-March and the US dollar has fallen back from highs reached around the same time.
- For much of the quarter global equity indices continued to push higher in local currency terms, although sterling strength has cancelled out most of the gains for unhedged UK investors. Heightened fears of a Greek exit from the euro led to setbacks in June.
- The most notable feature of global equity sector performance has been the weakness of Utilities – a sector often sensitive to movements in bond yields.

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- The monthly rise in UK property indices has recovered from the subdued levels of January and February, but the momentum of the rally does seem to have slowed a little since the end of 2014.

Manager comments and recommendations

The table below sets out the manager ratings for the Fund's investment managers.

Manager	Rating *				
L&G - Global Equities	Red	Orange	Yellow	Green	Black
Lazard - Global Equities	Red	Black	Orange	Yellow	Green
Longview - Global Equity	Red	Orange	Yellow	Green	Black
State Street - Fundamental Indexation	Red	Orange	Yellow	Green	Black
L&G - UK Equities	Red	Orange	Yellow	Green	Black
Newton - Absolute Return	Red	Orange	Yellow	Green	Black
Ruffer - Absolute Return	Red	Orange	Yellow	Green	Black
L&G - 5yr ILG	Red	Orange	Yellow	Green	Black
M&G - Bonds	Red	Orange	Yellow	Green	Black
Schroder - Property	Red	Orange	Yellow	Green	Black

Manager Updates

In February we took the decision to downgrade our rating on **Lazard's** Global Thematic Equity strategy from '3 - On Watch' to '2 - Sell – review options'. We remain comfortable with Lazard's structure as an independent team focused on a single, unconstrained strategy and building portfolios with low turnover based on the portfolio managers' long term views. Unfortunately we have lost confidence in the Lazard team's ability to execute this approach effectively. Our loss of confidence stems from our belief that:

- The team's portfolio positioning has given the strategy a de facto macroeconomic stance which is not consistent with building a well-diversified approach informed by the thematic investment philosophy;
- The multi-sector, wealth creation themes are too diverse to give Lazard a sustained competitive advantage and the team's ability to add value through the selection of narrower, focused themes appears to have deteriorated (albeit we accept some of these are aimed at mitigating macroeconomic risk);
- While Global Thematic's portfolio positioning may see a transitory benefit from a possible US rate rise in 2015, we attach a relatively low probability to the strategy receiving sustained support from a meaningful tightening of global financial markets in the short to medium term.

A separate paper provides additional rationale behind the downgrade and sets out potential alternatives to Lazard the Fund may wish to consider.

Newton recently announced that its CIO, Simon Pryke, is leaving the firm. Pryke has been in the role for just over 3 years and has been involved in many of the recent organisational changes at the firm. The pace of these changes is expected to slow and Pryke apparently wants to continue in a more strategic / managerial role than Newton can now offer. Although this is a surprise and seems a little abrupt, we expect minimal direct impact at the portfolio management level from his departure (Pryke was not directly involved in the management of portfolios). There will be no direct CIO replacement. Instead Charles French, who has been with Newton for 15 years, will assume a Head of Investment role, which will focus on the successful functioning of the investment process; he will report to Chief Executive Officer, Helena Morrissey. There will be no change to the investment process as a result of Pryke's departure and French's appointment. At this point **all our Newton ratings are unchanged by this news.**

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Asset Allocation

Set out below is the Fund's strategic target and actual allocations at the end of Q1 2015 and at the 31 May.

Mandate	Value (£m)	Proportion (%)		Value (£m)	Proportion (%)	
	Q1 2015	Actual	Target	31-May	Actual	Target
L&G - Global Equities	216.4	7.9%	8.0%	216.8	7.8%	8.0%
Lazard - Global Equities	410.4	15.0%	15.0%	417.2	15.0%	15.0%
Longview - Global Equity	174.8	6.4%	5.0%	175.8	6.3%	5.0%
State Street - Fundamental Indexation	291.2	10.6%	10.0%	292.7	10.5%	10.0%
L&G - UK Equities	271.6	9.9%	12.0%	283.7	10.2%	12.0%
Newton - Absolute Return	250.1	9.1%	10.0%	250.4	9.0%	10.0%
Ruffer - Absolute Return	257.1	9.4%	10.0%	263.8	9.5%	10.0%
L&G - 5yr ILG	144.6	5.3%	5.0%	143.8	5.2%	5.0%
M&G - Bonds	180.8	6.6%	6.5%	179.2	6.4%	6.5%
Schroder - Property	300.5	11.0%	10.0%	306.1	11.0%	10.0%
M&G - Infrastructure Fund	33.5	1.2%	1.0%	39.1	1.4%	1.0%
UBS - Infrastructure	22.1	0.8%	1.0%	20.8	0.7%	1.0%
Adams Street - Private Equity	83.3	3.0%	2.8%	81.9	2.9%	2.8%
HarbourVest - Private Equity	70	2.6%	2.8%	69.0	2.5%	2.8%
M&G - UK Financing Fund	10.7	0.4%	1.0%	10.7	0.4%	1.0%
Cash account	25.4	0.9%	0.0%	28.2	1.0%	0.0%
Total	2,742.4	100.00%	100.00%	2,779.3	100.00%	100.00%

Source: Investment managers, Northern Trust

The Fund's assets have increased by £36.9m over the two months to 31 May 2015. Allocations are broadly unchanged as at 31 May 2015, following the quarter end. The allocation to absolute return funds remains underweight its target by 1.5% and the allocation to L&G UK equities is also underweight the strategic target. This is offset by the 1% overweight to Schroder's multi-manager property mandate and the current cash holdings.

Performance to the end of May is provided below (where available).

Mandate	2 months to 31 May			12 months to 31 May 2015		
	Fund	Benchmark	Relative	Fund	Benchmark	Relative
L&G - Global Equities	0.2%	0.2%	0.0%	16.4%	16.3%	0.1%
Lazard - Global Equities	1.8%	0.2%	1.6%	18.4%	16.3%	1.8%
Longview - Global Equity	0.7%	0.0%	0.8%	27.4%	15.5%	10.3%
State Street - Fundamental Indexation	0.5%	0.6%	-0.1%	12.6%	12.6%	0.0%
L&G - UK Equities	4.4%	4.4%	0.0%	7.6%	7.5%	0.1%
Newton - Absolute Return	0.0%	0.7%	-0.8%	5.2%	4.4%	0.7%
Ruffer - Absolute Return	2.6%	0.1%	2.5%	14.5%	0.5%	13.9%
L&G - 5yr ILG	-0.5%	-0.5%	0.0%	n/a	n/a	n/a
M&G - Bonds	-1.0%	-1.2%	0.1%	7.6%	6.3%	1.2%
Schroder - Property	n/a	n/a	n/a	n/a	n/a	n/a

Source: Investment managers, Northern Trust

Schroders were unable to provide fund and benchmark performance for the 2 months following Q1 2015, as several of the underlying funds within the multi-manager mandate are only priced on a quarterly basis. Therefore they do not feel that part quarter performance will be particularly meaningful or portray an accurate representation.

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Over the two months following the Q1 quarter end, the majority of the Fund's mandates have outperformed or are in line with their respective benchmarks. Newton's Real Return Fund has delivered a small underperformance of 0.8% over the previous two months but remains ahead of its target over 12 months to 31 May 2015. The L&G index-linked gilts holdings and the M&G bond mandate delivered negative absolute returns as yields increased following the quarter end.

Summary

The key points to note are:

- Lazard have been downgraded to a rating of 2 – 'Sell no immediacy';
- Newton have announced that the CIO Simon Pryke will be leaving the firm. Our rating for the Real Return Fund is unchanged following this news at the current time;
- As at 31 May 2015, asset allocation remains broadly in line with allocations as at 31 March 2015;
- In the 12 months to the end of May there has been significant outperformance from Longview (global equities) and Ruffer (multi-asset absolute return);
- Newton's Real Return Fund underperformed the benchmark during the two months to 31 May 2015; and
- All other mandates outperformed or were in line with their respective benchmarks during the two months to 31 May 2015.

We look forward to discussing this at the upcoming meeting.

Linda Selman

Partner

June 2015

For and on behalf of Hymans Robertson LLP

Notes

Market returns

Percentage total returns in local currency (\$ for Commodities and Hedge funds). Source: Datastream; indices as shown below.

Equities		Bonds	
UK	FTSE All-Share	Conventional gilts	FTSE-A UK Gilts All Stocks
Overseas (developed)	FTSE World	Index-linked gilts	FTSE-A UK Index Linked Gilts All Stocks
Emerging Markets	FTSE Emerging	UK credit	iBoxx Non Gilts All Maturities
Property	IPD Monthly	Overseas Government	JP Morgan Global
Hedge Funds	DJ CS Hedge Fund/Core Hedge Fund	Commodities	S&P GSCI Light Energy

General Risk Warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets.

Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.