

REPORT PREPARED FOR

**London Borough of Bromley
Pension Fund**

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This quarterly report by your adviser, Alick Stevenson, of AllenbridgeEpic Investment Advisers (AllenbridgeEpic), provides a summary of performance and an analysis of the investments of the London Borough of Bromley Pension Fund for the three months ending 31 December 2013.

Market Summary 4th Quarter 2013

“The first rule is not to lose money. The second rule is not to forget the first rule”

Warren Buffett

News in December that the Federal Reserve was reducing the \$85bn monthly bond buying programme from January 2014 to **just** \$75bn per month was accepted by the markets as an “early Christmas present” and accordingly the markets moved higher and bond yields fell back. Since then however, markets have drifted in moderate trading, lacking positive news to take them to new “highs”.

Interestingly, this news regarding tapering was met with widespread equanimity by the markets, in stark contrast to the subsequent volatility of May and June 2013 when the markets “misinterpreted” Bernanke’s words of wisdom.

It would seem logical that the markets will test Central Bank resolve on interest rates over coming months, a challenge which may create more significant market volatility, as the two protagonists vie with each other over the timing and extent of any rate increase.

Meanwhile in Europe, very little has changed since the previous quarter, although the trade imbalances as recorded in France (the deficit) and in Germany (the surplus), continue to grow a disparity which suggests further future volatility in the economic and political relationships between the two nations.

In the UK, economic news has generally been mildly positive with sterling picking up strength against the US dollar. UK RPI fell to 2.2% at the end of the year, down 0.9% from 31 December 2012.

As far as general market investment performance is concerned, almost all regional equity indices posted significant gains over the last calendar year, with only Emerging Markets and the small Russian index posting negative returns. Interestingly, over the last five years, emerging markets produced a total return of around 100% despite that negative return in 2013. Fixed income indices also showed negative returns but typically much less negative than those of 2012. Only High Yield (below investment grade) showed a positive return. In fact, European High Yield has shown a 150% total return over five years. This amazing performance made possible by central banks keeping interest rates very low and thus the cost of refinancing has been relatively benign.

Key issues facing the markets as we move into 2014 include:

Central banks’ ability to manage “tapering” without derailing the nascent recovery and at the same time keeping the markets “happy”

Global growth continues to improve slowly and broadly

No significant fiscal problems in the Eurozone

No market perceived “bubbles” in asset prices leading to increased volatility and potential market declines

Executive Summary

The fund value as at 31 December 2013 was £618.8m a net increase in value of £17.1m since 30 September 2013 (£601.7m) and significantly higher than the fund value of £526.00 at the end of December 2012.

The Second Phase of the investment reorganisation that of moving equity assets from regional, pooled and segregated mandates to global equity mandates was concluded on 20 December 2013. A separate report is included in these papers.

The Third Phase of the investment reorganisation that of moving the fixed income assets to global absolute return or other similar funds, commenced in November 2013. A separate report is included with these papers.

Of the managers whose investment portfolios did not change dramatically during the quarter, the Baillie Gifford DGF fund achieved an investment return of 2.4%, however for the rolling twelve months the fund has returned 5.4% and since inception (5 December 2012) a solid 5.9% against a benchmark of 4.0%. In parallel, the Standard Life GARS portfolio had a quarterly return of 3.6% and a very solid 7.0% for the rolling twelve months.

Fidelity Global Aggregate fixed income portfolio also did well with returns of 1.4% (1.2%) for the quarter, -1.1% for the rolling twelve months against a benchmark of -1.7% and 6.8%pa (5.8%pa) over the rolling three year period.

Fund Value

Manager name	asset class	Value 30 Sep £m	Actual % v Fund	Value 31 Dec £m	Actual % v Total Fund	SAA
Standard Life	DGF	26.0		26.9		
Baillie Gifford	DGF	26.0		26.6		
sub total DGF			8.6	53.5	8.6	10.0
Baillie Gifford	Equities	272.1		203.5		
	Global Equity			14.9		
Fidelity	GE ETF	170.7	73.6			
	Equities					
MFS	Global Equity			122.7		
BlackRock	Global Equity			121.8		
sub total GE				462.9	74.8	70.0
Fidelity	Fixed Income	52.0		52.9		
Baillie Gifford	Fixed Income	44.1		44.1		
sub total FI			16.0	97.0	15.7	20.0
Fidelity	Cash	0.8		3.8		0.0
Baillie Gifford	Cash	10.0		1.6		
sub total Cash			1.8	5.4	0.9	0.0
Total		601.7	100.0	618.8	100.0	100.0

Source: BlackRock, Baillie Gifford, Standard Life, MFS and Fidelity

As far as the Strategic or long term asset allocations are concerned the fund remains overweight equities and underweight DGF and fixed interest. These over and underweight positions will be closely monitored and adjusted following completion of the Phase 3 Fixed Income restructuring currently in its early stages.

Fund Investment Performance Highlights

Please note that the WM Quarterly report was not available at the time this report was completed and thus no charts have been added to this report either here or in the specific investment manager reports.

This delay is due to the incorporation of the new investment managers and the transition of assets from Baillie Gifford and Fidelity requiring changes to their own internal benchmarks.

Normal service will be resumed with effect from the first quarter 2014

Fund performance for the quarter under review was made more complex by the significant transition of equities between various managers. The portfolios that continued during the transition process are reported on more fully elsewhere in this report.

Fidelity fixed income portfolio again performed well

Both Baillie Gifford and Standard Life diversified growth funds performed well

Manager Changes

There were no changes in senior investment personnel which would affect the running of existing portfolios

Fund Governance and Voting

These reports will recommence with the 1st Quarter 2014 and will reflect the global nature of the new portfolios

Investment Manager Reviews

Baillie Gifford Global Equity Portfolio

This new portfolio was funded as at 20 December 2013. A full review will be provided following the end of the first quarter 2014

Baillie Gifford Diversified Growth Fund

The fund has performed well since its inception in December 2012 generating a net return of 5.9%. For the 12 month period it has a return of 5.4% against the LIBOR based benchmark of 4%, and was ahead for the quarter by 1.4% (benchmark 1.0%).

Primary contributors in the fourth quarter were holdings in equities and high yield bonds, although emerging market equities and gold had a negative impact. Since the previous quarterly report the fund has reduced its holdings in listed equities, commodities, absolute return and insurance linked securities in favour of increased weightings in investment grade

and high yield bonds and cash which increased from 6.0% to 10% of the overall assets of the fund.

Holdings in Insurance linked securities (“ILS”) were cut back as the manager sold securities into a significant demand from other investors, thus reducing overall holdings and booking profits on assets, some of which had been held since 2008.

BlackRock Global Enhanced Equity Fund

This new portfolio was funded as at 20 December 2013. A full review will be provided following the end of the first quarter 2014

Fidelity Global Aggregate fixed Income Portfolio

A good quarter for the manager as corporate bonds outperformed government bonds. Whilst the three year return of 6.8%pa is an excellent rolling return, this will gradually reduce as the lower margins and impact of investor demand remove strong quarterly investment performances from the measured period.

In terms of credit ratings, the fund has nearly 82% invested in AAA, AA and A rated bonds with almost all the balance in BBB rated bonds. All exposure to high yield, one of the key drivers of enhanced returns in the past, has now been liquidated. Largest sectoral holding is in banks and brokers with 11.8%, followed by Communications with 6.9% both of which are overweight to the benchmark. The main holding is in US treasuries with 44.1% (benchmark 50.1%) of the fund invested. Looking forward the manager is optimistic for growth rates, although the potential to achieve growth rates similar to longer term historic averages is restricted. With interest rates expected to be held down for an extended period, return expectations from gilts remain low. Corporate bond yields remain firm as corporate balance sheets are healthy.

MFS Global Equity

This new portfolio was funded as at 18 December 2013. A full review will be provided following the end of the first quarter 2014

Standard Life GARS Fund

A formal presentation of the investment results to date and the asset allocation mix will be provided at the meeting on 11 February 2014.

Asset Allocation Review

Global Equities

A new table will replace the old aggregated fund asset allocations and will highlight the different investment thought processes through and by which the three global equity managers allocate risk. This will be available from the 31 March 2014 quarter

Diversified Growth Funds

The chart on the following page highlights the asset allocation differences between Baillie Gifford and Standard Life in sourcing investment returns

	Baillie Gifford %	Baillie Gifford £m	Standard Life %	Standard Life £m	Total DGF £m	Total DGF %
Values at 31 December 2013		26.6		26.9	53.5	
Asset Class						
Global equities	15.6	4.1	33.8	9.1	13.2	24.8
Private equity	3.2	0.9			0.9	1.6
Property	1.9	0.5			0.5	0.9
Global REITS			5	1.3	1.3	2.5
Commodities	3.8	1.0			1.0	1.9
Bonds						
High yield	12.3	3.3	6.8	1.8	5.1	9.5
Investment grade	9.0	2.4	4.9	1.3	3.7	6.9
Emerging markets	12.5	3.3			3.3	6.2
UK corp bonds			4.9	1.3	1.3	2.5
EU corp bonds						
Government	5.2	1.4			1.4	2.6
Global index linked					0.0	
Structured finance	10.4	2.8			2.8	5.2
Infrastructure	3.4	0.9			0.9	1.7
Absolute return	5.9	1.6			1.6	2.9
Insurance Linked	5.9	1.6			1.6	2.9
Special opportunities	0.6	0.2	4.5	1.2	1.4	2.6
Active currency	0.3	0.1			0.1	0.1
Cash	10.0	2.7			2.7	5.0
Cash and derivatives			40.1	10.8	10.8	20.2
Total	100.0	26.6	100.0	26.9	53.5	100.0

numbers may not add due to roundings

Source: Baillie Gifford and Standard Life

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