AllenbridgeEpic
investment advisers

APPENDIX 6

REPORT ON QUARTER ENDED 30TH JUNE 2014 PREPARED FOR

London Borough of Bromley Pension Fund

1 August 2014

Alick Stevenson
AllenbridgeEpic Investment Advisers Limited (AllenbridgeEpic)

Alick.stevenson@allenbridgeepic.com
www.allenbridgeepic.com

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 30 June 2014.

Market Summary 2nd Quarter 2014

"Know what you own, and know why you own it"

Peter Lynch
Investment Manager

There was little to be joyful about during the second quarter of this year.

The conflict in the Ukraine continued, the Middle East kicked off a fundamentalist action in Iraq and tensions in the Gaza also threatened stability.
Populist political successes in the European elections and the subsequent election of M Juncker as EU President (a renowned federalist) did little to improve markets which, in Europe, remained sluggish even after Sr Draghi's interest rate cuts.

The Federal Reserve continued to reduce its bond buying activities by $10bn per month and in the UK, Governor Carney seemed to contradict himself by saying that interest rates would have to rise and then that "raising interest rates was probably the last line of defence". Such "deific and contradictory pronouncements" only serve to confuse market makers and investors alike.

In any event, equity markets generally moved upwards.

In the US the Dow moved through the 17,000 high point before retreating. The FTSE flirted with its fifteen year high and then also retreated. In Japan the market had a quarterly return of +4.3%, emerging markets +4.0% while the US and the UK returned 2.3% and 2.2% respectively. Europe ex UK was the poor relation with a return of just +0.1%.

On the bond markets, European issues were amongst the strongest performers over the quarter. Greek debt was in demand and in Spain, the 10 year issue traded, briefly, below its US equivalent, for the first time since 2010.

Volatility, or the "fear index" traded down to the low 10% levels, last seen before the Lehman crisis, before moving significantly higher as global stability took a major turn for the worse ending July at 17.0%. (The twelve month range is 20% to 10%)

It is however, interesting to note that seven years on from the first flare up in the global markets, levels of debt are little changed, albeit more is now held by the central banks than the private sector, and whilst this situation continues under the "benign but watchful eyes" of the central banks, investors should look at their current investment strategies and consider if the assets within and their percentage allocations are fit for purpose. Should they consider changing their asset mix then they should choose their assets wisely. In this context, whilst interest rates are expected to move upwards, this is not necessarily a signal for equity markets to decline; it is the reason (s) why interest rates move upwards which is the key.

The economist Hyman Mynsky once famously observed that "long periods of stability are ultimately destabilising" implying perhaps that these "goldilocks" conditions may not last forever and that using the same comparison, the "big bad wolf" may be lurking around the corner.

A further market update on events since 30 June 2014 will be given verbally at the next meeting.

Executive Summary

The fund value as **at 30 June 2014 was £636.7m a net increase** in value of 10.6m since 31 March 2014 (£626.1m) and significantly higher than the fund value of £601.7m at the end of June 2013.

The lack of directional movement in the major markets, coupled with the number of crises in the world meant that the fund produced a small negative return at total fund level. For the quarter the fund was behind the benchmark by 0.5%, flat over the twelve months but remains a solid 1.3%pa ahead over the rolling three years (9.0%pa v 7.5%pa).

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.

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.

Fund Value as at 30 June 2014

Manager Name		Asset Class	Value 31-Mar-14 £m	Actual % of Fund		Value 30-Jun-14 £m	Actual % of Fund		Strategic Asset Allocation
Baillie Gifford**		DGF	26.8			43.0			
Standard Life		DGF	27.0			27.3			
Sub total DGF			53.8	8.5		70.3	11.0		10.0
Baillie Gifford			207.8			208.9			
BlackRock			122.5			126.5			
MFS			123.5			125.5			
BG ETF**			15.2			0.0			
Sub total GE			469	74.3		460.9	72.4		70.0
Baillie Gifford			45.2			46.1			
Fidelity			54.6			59.7			
Sub total FI			99.8	15.8		105.8	16.6		20.0
BG			5.1						
Fidelity			3.8						
Sub total cash			8.9	1.4		0.0	0.0		
Fund Totals			631.5	100.0		637.0	100.0		100.0

** The global equity ETF funds were transferred to Baillie Gifford DGF in a final "top up" transaction in the final step to complete Phase 2 of the 3 Phase Fund restructuring programme commenced in 2012

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

Fund Investment Performance Highlights

Fund performance for the quarter under review is shown by manager and at total fund level

	Mkt Val (GBP 1000)	% of Fund	Latest Quarter	12 Months	3 Years	5 Years	10 Years
Multi Asset							
BAILLIE GIFFORD & CO	208,926	32.8	0.3	9.5	9.0	15.0	10.2
LB OF BROMLEY BGIFFORD BM			2.6	9.6	7.4	12.3	8.5
			-2.3	-0.1	1.5	2.4	1.6
Bonds - Sterling							
FIDELITY INVESTMENT SERVICES LIMITED	59,578	9.4	1.9	9.7	9.5	13.8	9.7
LB OF BROMLEY FIDELITY BM			1.6	8.0	7.5	12.2	8.1
			0.3	1.6	1.9	1.5	1.5
BAILLIE GIFFORD & CO	46,134	7.2	2.3				
LB of Bromley B Gifford Fixed Interest Benchmark			1.6				
			0.6				
Structured Products							
BAILLIE GIFFORD & CO	43,045	6.8	2.2	6.4			
BANK OF ENGLAND BASE RATE + 3.5%			1.0	4.0			
			1.2	2.3			
STANDARD LIFE	27,329	4.3	1.4	5.3			
GBP 6 MONTH LIBOR + 5%			1.4	5.6			
			0.0	-0.3			
Equity - World							
BLACKROCK	126,462	19.9	3.3				
MSCI AC WORLD GDR			2.6				
			0.6				
MFS	125,265	19.7	1.8				
MSCI AC WORLD NDR			2.4				
			-0.6				
TOTAL FUND							
TOTAL COMBINED	636,738	100.0	1.6	9.6	9.0	14.3	9.8
LB OF BROMLEY STRATEGIC BENCHMARK			2.3	9.6	7.5	12.3	8.4
			-0.6	0.1	1.3	1.8	1.3

WM investment services

Overall, the fund had a small negative performance to the benchmark for the second quarter, the majority of which came from poor stock selection in global equities. Comments on this poor stock selection are contained within the separate Investment Manager reviews below:

Manager Changes

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

Fund Governance and Voting

Voting and governance matters are covered in some detail within the various investment Manager reports provided to the members under separate cover.

Investment Manager Reviews

GLOBAL EQUITY PORTFOLIOS

Baillie Gifford Global Alpha (segregated)

This new portfolio was funded as at 20 December 2013.

Fund positioning was little different from the previous quarter with just minor changes; previous quarter numbers in brackets. At the end of June 2014 the global equity fund was invested across 24 (24) countries and held 98 (99) different investments. These investments were spread over 9 (9) sectors and encompassed 43 (42) differing industries, thus providing a broadly diversified set of assets. It is worth noting that the active money within this portfolio is currently running at 92% (91%). This implies that the fund is not holding benchmark or index weightings relating to stocks making up the index and reflects the active stock picking philosophy of the manager.

With only two quarters since inception the manager had a loss for the quarter with a return of just 0.3% return versus the benchmark of 2.3%.
In terms of regional allocations Baillie Gifford is underweight North America (45.8% v 59.2%) and Developed Asia Pacific (9.3% v 5.0%) but is running a significant overweight to Emerging Markets +13.4% against an index weighting of zero.

Reinforcing the “active money” style, the top ten holdings account for nearly 22% of the total portfolio. Prudential at 3.1%, Naspers 2.8%, Royal Caribbean Cruises at 2.6% make up the top three names whilst, Nestle, TD Ameritrade and Samsung take the bottom three positions with 1.8%, 1.8% and 1.7% respectively.

BlackRock Ascent Life Enhanced Global Equity Fund (pooled)

This new portfolio was funded as at 20 December 2013

The manager can invest across the whole of the ACW Index and as a result held approximately 755 stocks at the end of the quarter. The fund out performed its benchmark this quarter by 0.8% (benchmark 3.2% v 2.4%).

In their 1Q 2014 report Blackrock held 949 stocks but made no comment in their 2Q report. When challenged their response was as follows:

Alick

It is correct that the number of holdings have dropped from 949 to 755 over the Q2 2014. Please see below the reasoning behind this change.

In early Q2 we made some allocation changes to our global model and also imposed tighter constraints at the industry/country level. This was in response to the drawdown we had observed in trending strategies over Feb-April, which was most severe in industry country positions. To summarize-

- We reduced the allocation to macro/thematic insights, which are predominantly expressed by industry & country over/underweights.

- We also reduced the maximum deviation from the index weight at the country/industry level from 3% to 2.5%.

- A commensurate increase in allocation to stock specific insights, which drive individual stock positions.

- To still achieve our active risk target, while taking less country/industry risk, the number of individual positions needed to be reduced i.e. less positions, more stock specific risk

My response:

Ahsan, I welcome the explanation but am concerned that you, (BlackRock), did not deem this a significant change worthy of explanation to clients in the 2nd quarter report.

No doubt you will flag to your management that there are some funds (clients) that have officers or advisers that actually read your reports and challenge the differences and that leaving out pertinent and significant changes may cause clients to question BlackRock's commitment to transparent reporting.

MFS Global Equity Fund (segregated)

This new portfolio was funded as at 18 December 2013.

MFS currently invests in 15 (16) countries and has 110 (113) holdings. This contrasts with the benchmark of 1,611 holdings spread across 24 countries. Since inception the fund has returned 4.3% (net) against the benchmark of 5.2% for a small underperformance of 0.6%.

Looking through the country and sector weights shows that the fund is currently underweight North America (51.0% v 59.2%) and Asia Pacific ex japan (1.2% v 5.0), but overweight Europe ex UK (+2.0%) UK (+2.4%) and japan +4.5%). The fund is also running a small, +1.2% overweight in emerging markets.
Sectorally, the fund is significantly overweight in Consumer staples (+20.1% v 9.7% (19.6% v 9.8%), with small overweights in Industrials, telecommunication services and Healthcare. These overweights are being "funded" by underweight positions in Financials, Consumer Discretionary, Utilities, Energy and Materials.
In terms of largest holdings KDDI Corporation with 2.5% of the portfolio and Johnson & Johnson at 2.3% are the two largest holdings. With KAO Corporation and Danone at 1.7% taking the ninth and tenth positions.

Global equity crossholdings

Of the top ten holdings by manager only two stocks are held by more than one manager and represent just 0.17% of the total fund of £637m

JP Morgan 1.8% by BlackRock and 1.8% by MFS (Value of total holdings £6.0m)
Nestle 1.8% by Baillie Gifford and 2.0% by MFS (value of total holdings £4.8m)

DIVERSIFIED GROWTH FUNDS

Baillie Gifford Diversified Growth Fund

The fund has performed well since its inception in December 2012 generating a net return of 5.9% against the benchmark of 4.0%. For the 12 month period it has returned 6.4% against the LIBOR based benchmark of 4%, and was ahead for the quarter by 1.1% (benchmark 1.0%).

The primary contributor to performance in the first quarter was Emerging market bonds followed by holdings in equities, investment grade bonds and infrastructure, although absolute return investments again had a negative impact.

There were few major changes to the overall asset allocations over the quarter, the exceptions being an increase in structured finance from 9.8% to 12.3%, absolute return up from 4.9% to 7.7%. These additions were primarily funded from cash holdings down from 9.5% to 5.8% and a small 2.0% reduction in high yield bond allocations.

One of the primary directives for the fund, and one closely followed, is to keep the volatility within target. At the end of the quarter the current figure was 5.6% (6.5%) well within the upper ceiling of +10%.

Standard Life Global Absolute Return Fund

GARS has delivered strong results for the 12 months with a return of 5.3% versus a benchmark of 0.7%, although less strong for the quarter with a return of 1.4% against the benchmark of 0.2%.
Positive contributions from directional currency investments, global equities and global REITs investments were offset by losses on relative value investments. Volatility within GARS was just 3.9% for the quarter.

Asset allocations at the end of the first quarter were almost exactly the same as those at the end of the fourth Quarter 2013. The only significant change was a new investment in Emerging Market bonds funded by small reductions in equities and cash and cash equivalents.

In terms of construction the fund is running some 30 different strategies with approximately 36% (40%) invested in directional, 35% (35%) in market return assets, 27% (25%) in relative value and just 2% in security selection.

Baillie Gifford has maintained its much lower allocation to global equities, but has retained a higher allocation to both high yield and emerging market bonds in contrast to Standard Life which holds just over 37% of its assets in derivative based investments.

The chart below 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 %
Value at 30 June 2014			43.0		27.3	70.4	
Asset Class							
Global equities		15.1	6.5	35.4	9.7	16.2	23.3
Private equity		2.5	1.1			1.1	1.6
Property		2.0	0.9			0.9	1.2
Global REITS				5.1	1.4	1.4	2.0
Commodities		6.7	2.9			2.9	4.2
Bonds				4.9	1.3	1.2	1.7
High yield		10.5	4.5	5.0	1.4	5.9	8.5
Investment grade		9.2	4.0			4.0	5.7
Emerging markets		13.7	5.9	3		5.9	8.5
UK corp bonds				4.5	1.2	1.2	1.8
EU corp bonds				4.9	1.3	1.3	1.9
Government		5.0	2.2			2.2	3.1
Global index linked					0.0	0.0	0.0
Structured finance		12.3	5.3			5.3	7.6
Infrastructure		4.1	1.8			1.8	2.5

Absolute return		7.7	3.3			3.3	4.8
Insurance Linked		4.8	2.1			2.1	3.0
Special opportunities		0.6	0.3		0.0	0.3	0.4
Active currency		0.0	0.0			0.0	0.0
Cash		5.8	2.5			2.5	3.6
Cash and derivatives				37.2	10.2	10.2	14.6
Total		100.0	**43.0**	100.0	**26.5**	**69.4**	100.0

numbers may not add due to roundings

Source: Baillie Gifford and Standard Life

FIXED INCOME PORTFOLIOS

Fidelity Global Aggregate fixed Income Portfolio

Another good quarter for the manager as corporate bonds once again outperformed government bonds. Despite being just ahead over the quarter +0.3% to the benchmark, the three year return of 9.5%pa (benchmark 7.5%pa) continues to held up well, over time this is likely to erode as lower margins and impact of investor demand replace past strong quarterly investment performances from the measured period.

In terms of credit ratings, the fund has nearly 70% invested in AAA, AA and A rated bonds with some 25% in BBB rated bonds. The manager has maintained a small position (3.0%) in high yield bonds and holds the remaining 2% in a mix of cash (0.4%) and unrated investments.

There has been very little change in sectoral allocations with US treasury assets accounting for approximately 40% of the portfolio. Overweight positions in the Financial Services, Communications and Insurance sectors are offset by underweights in Supranationals and Sovereign assets and Utilities.

The portfolio has maintained its benchmark duration of 8.6 years and has a running yield of just 3.6%.

Baillie Gifford Aggregate Plus Portfolio

The transition to the new portfolio was completed during the second quarter and as a result it is too soon to show performance or comment on asset allocations. A full report on the new fund together with a comparator to the Fidelity Global Aggregate Portfolio will be included in the 3rd Quarter 2014 INVESTREP.

Alick Stevenson
Senior Adviser
AllenbridgeEpic Investment Advisers