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AVON PENSION FUND

ANNUAL INVESTMENT REVIEW TO 31 MARCH 2015

MAY 2015

MARSH & McLENNAN COMPANIES

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- Care should be taken when comparing private equity / infrastructure performance (which is generally a money-weighted performance) with quoted investment performance (which is generally a time-weighted performance). Direct comparisons are not always possible.
- Performance figures are gross of fees and sourced from WM Services, unless stated otherwise.

Contents

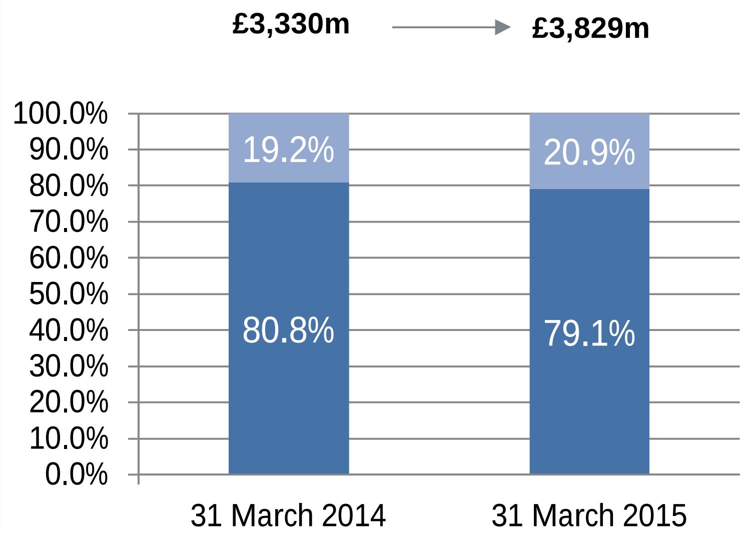
Section 1

Executive Summary

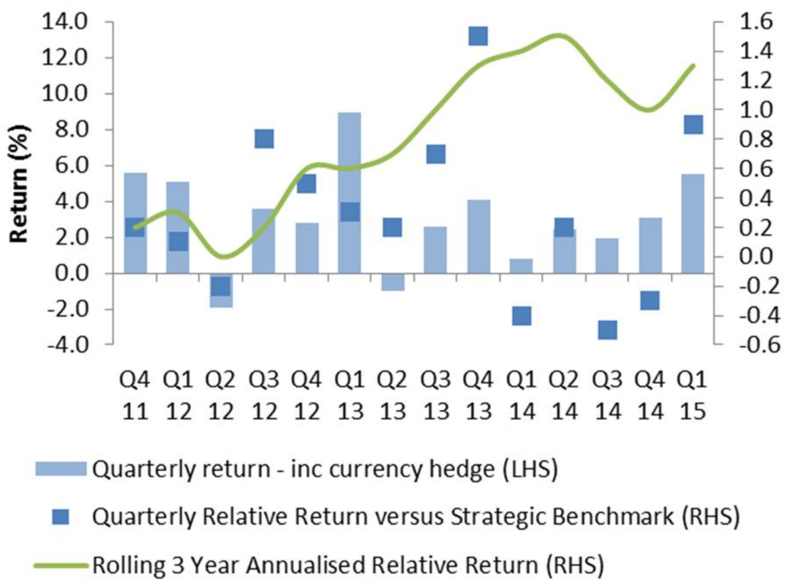
Executive Summary

	3 months (%)	1 year (%)	3 years (% p.a.)
Total Fund (inc currency hedge)	5.5	13.5	11.2
Total Fund (ex currency hedge)	5.4	13.3	11.0
Strategic Benchmark (no currency hedge)	4.6	13.2	9.9
Relative (inc currency hedge)	**+0.9**	**+0.3**	**+1.3**

Asset Allocation



Excess Return Chart



Commentary

Over the year total Fund assets (including currency hedging) increased by just under £500m.

This increase was largely due to the strong performance of most asset classes in particular UK bonds, overseas equity and property, together with contributions paid over the year.

At a strategic level, the Fund was within the tolerance ranges in the Statement of Investment Principles for all asset classes with the exception of developed market equities (although this overweight allocation will be reduced once the investments in the new Infrastructure and Hedge Fund mandates is drawn down).

Executive Summary

This report has been prepared for the Avon Pension Fund ("the Fund"), to assess the performance and risks of the Fund's investments.

Funding level

- The estimated funding level fell by c7% to 78% over the year to 31 March 2015, with the rise in asset values outpaced by the increase in liabilities caused by the fall in real and nominal gilt yields (which increased estimated liabilities by around £750m).

Fund performance

- The value of the Fund's assets increased by c. £500m over the year, to £3,829m at 31 March 2015. The total Fund returned 13.5% (13.3% excluding Record's currency hedging mandate), as a result of positive returns from all funds except Man and Signet. This marginally outperformed the strategic benchmark return of 13.2% (excluding currency hedging) due to asset allocation in overseas equities (where an overweight position was held in assets that outperformed the total strategic return), and multi-asset and hedge funds (where the Fund was underweight assets which underperformed the strategic return).

Strategy (index returns versus strategic returns)

- Global (developed) equity returns over the last three years at 14.2% p.a. have been significantly ahead of the assumed strategic return of 8.25% p.a. from the strategic review in March 2013. We are neutral in our medium term outlook for developed market equities (over the next one to three years), and expect returns to be more modest looking ahead over the next three years.

Strategy (continued)

- The three year return from emerging market equities has fallen to 3.7% p.a. from 4.8% p.a., with the Q1 2012 performance (which dropped out of the index) being significantly higher than the Q1 2015 return. The three year return remains below the assumed strategic return (of 8.75% p.a.) as 2013 returns were affected by negative sentiment from slowing growth and the tapering of the US asset purchase programme, together with the negative impact of the strengthening USD on many emerging economies. Emerging markets have, however, rallied modestly post 31 March 2015 as sentiment gradually improves. As for developed markets, we are neutral in our medium term outlook for emerging market equities over the next one to three years.
- UK government bond returns over the three years to 31 March 2015 remain above the long term strategic assumed returns (with fixed interest gilts returning 10.0% p.a. against an assumed return of 4.5% p.a., and index-linked gilts returning 8.9% p.a. versus an assumed return of 4.25% p.a.) as investor demand for gilts remained insatiable. Whilst from an absolute return perspective, government bonds remain unattractive due to the low yields available, their value in the context of the overall portfolio is important from a liability risk management perspective.
- The strong returns from gilts also means the present value of the Fund's liabilities will have increased significantly over the three year period as a result of the falling bond yields (which will have resulted in a lower discount rate).
- UK Corporate bonds also performed strongly, returning 8.8% p.a. over the three year period against the assumed return of 5.5% p.a., while property returns continue to increase above the assumed strategic return of 7% p.a., driven by the economic recovery in the US and the UK. Looking forward, our medium term view for the prospects for corporate bonds remains unattractive, and we are encouraging clients to consider ways of expanding credit mandates (potentially via multi-asset credit).

Executive Summary

Strategy (continued)

- We have moved our rating for UK property from attractive to neutral over the year given the drop in yields and signs that the market is potentially moving beyond fair value in some parts (with ultra-prime central London assets in particular aggressively priced and rents back to pre-financial crisis levels).
- Hedge fund returns remain below long term averages and the strategic return of 6% p.a., as they are affected by low cash rates. With most listed assets looking close to fully valued if not fully valued, we would expect ‘alpha’ driven investments such as Hedge Funds and DGF to play an increasingly important role in return generation over the coming three years, particularly if ‘beta’ (i.e. market-driven) returns are lower looking forward.

Managers

- Absolute returns over the year were mixed, but generally positive in light of buoyant markets. The Fund’s global equity mandates in particular fared well, with Invesco returning 21.6% (1.3% above benchmark), and SSgA’s enhanced indexation Pacific Rim mandate returning 21.3% (against a benchmark of 19.4%). Weakest performance over the year was from the Fund of Hedge Fund mandates, with Signet returning -4.1% in a challenging environment for hedge funds.
- Over three years, all funds produced positive returns (with the exception of Signet), with Partners and Signet both failing to beat their benchmarks (although see comments on the measurement of Partner’s performance later). In addition, despite producing returns at least in line with benchmark, Schroder (Equity), and TT International failed to achieve their three-year performance objectives (with the remainder of the active managers achieving their objectives).

Executive Summary

Key points for consideration

- Over the coming year, the Fund will be reviewing its policies on rebalancing and the use of opportunistic assets / tactical asset allocation, together with reviewing the alignment of the Fund's assets and liabilities, and ways to better manage liability risk.

- Over the year, the Fund disinvested from the Barings Dynamic Asset Allocation Fund, following the departure of the leading portfolio managers (Percival Stanion, Andrew Cole and Shaniel Ramjee) to join Pictet.

  – Proceeds from the disinvestment were invested in the BlackRock multi-asset portfolio in such a way as to broadly replicate the underlying asset allocation of the DAAF.
  – In February 2015, the proceeds were invested in a new Diversified Growth mandate with Standard Life.

- The Fund has confirmed the appointment of IFM to manage the 5% allocation to infrastructure. This mandate is expected to be funded from the equity holdings.

- The Fund has also reviewed its hedge fund allocations, and is in the process of confirming the appointment of one manager (JPMorgan) to replace the existing mandates.

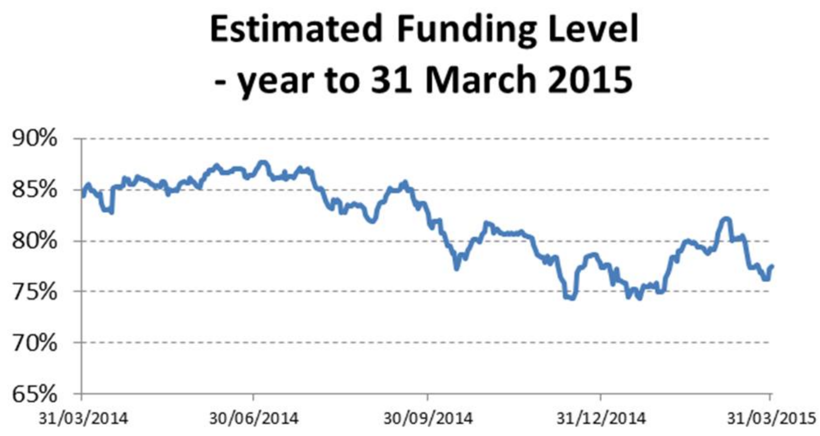
- The Schroder Global Equity mandate continues to underperform its performance objective. Performance should continue to be monitored to assess the impact of the changes implemented following the departure of Virginnie Maisonneuve (former portfolio manager and head of Global Equity).

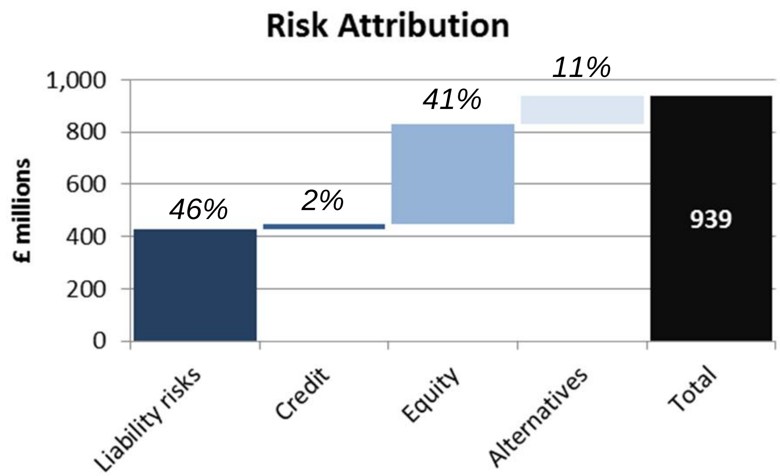
- The absolute performance of the Partners Property investment may be misleading given the significant cash flows, and the net internal rate of return (9.3% p.a. since inception) is a more meaningful measure, and is broadly in line with performance expectations.

Section 2

Consideration of Funding Level

Consideration of Funding Level
Year to 31 March 2015





The charts above illustrate the estimated progression of the funding level over the year to 31 March 2015 on the left hand side, and on the right the main risks the Fund is exposed to (which is why the funding position is volatile) and also the size of these risks in the context of the deficit position. The purpose of showing this chart is to provide an awareness of the risks faced and how they change over time and to initiate debate on an ongoing basis, around how to best manage these risks, so as not to lose sight of the “big picture”.

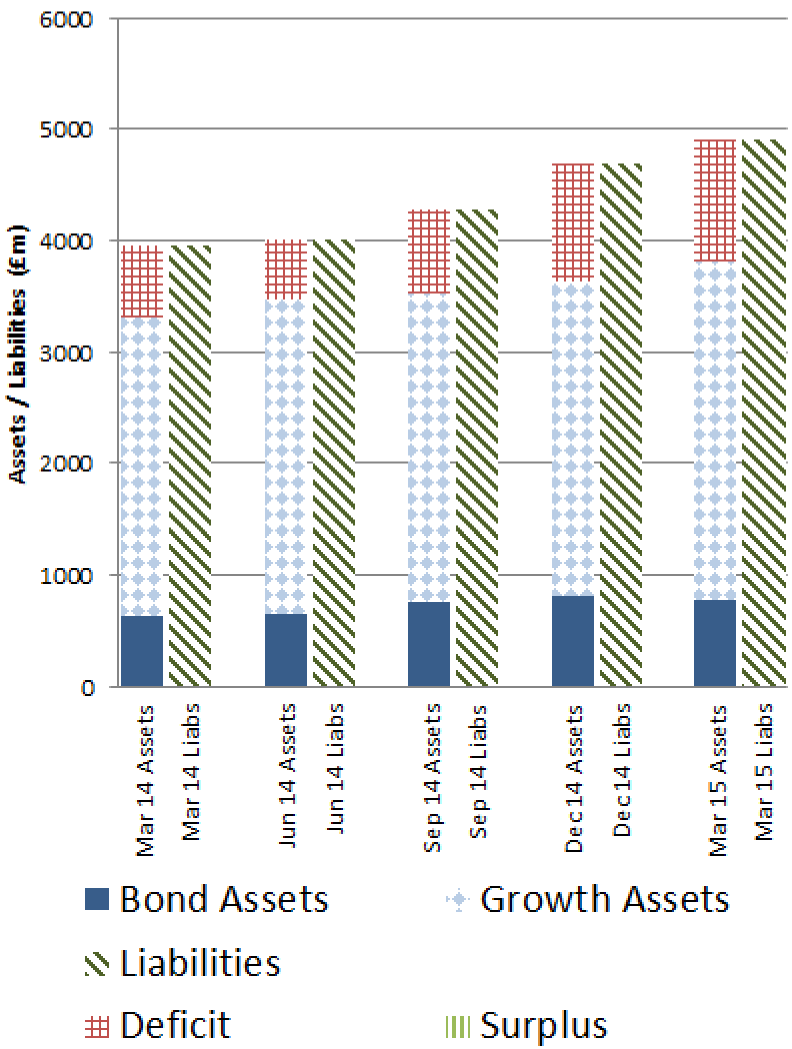
The black column on the right hand side of this chart shows the estimated 95th percentile Value at Risk figure over a one-year period. In other words, if we consider the worst case outcome which has a 1 in 20 chance of occurring, what would be the impact on the deficit relative to our “best estimate” of what the deficit would be in one years time. As at 31 March 2015, the chart shows that if a 1 in 20 “downside event” occurred, we would expect that in one year’s time, the deficit would increase by an additional **£939m** on top of the expected deficit at that time.

Each bar to the left of the black bar represents the contribution to this total risk from the primary underlying risk exposures (interest rates and inflation, changes in credit spreads, and volatility of equity markets and alternative assets). **It should be noted that while these figures indicate levels of volatility on the downside, there is also a potential upside benefit from taking these risks.**

Liability risks (i.e. interest rate and inflation) and equity market risk dominate as the two significant drivers of volatility. It is proposed that the liability risks are reviewed in greater detail as part of a comprehensive Risk Management Framework over the coming year, alongside the 2016 actuarial valuation, to ensure that the balance of risks taken is appropriate.

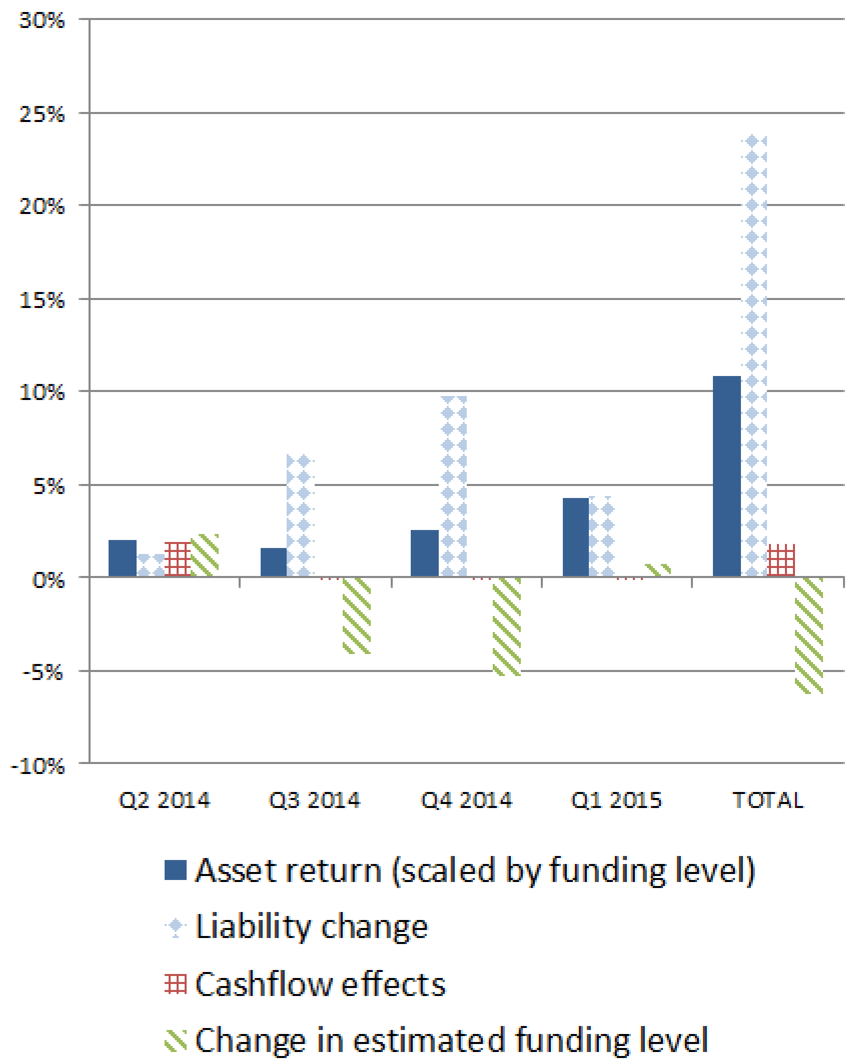
The VaR figures shown are based on approximate liability data rather than actual Fund cashflows, and are based on the strategic asset allocation. They are therefore illustrative only and should not be used as a basis for taking any strategic decisions.

Consideration of Funding Level
Asset allocation and funding level



- Based on market movements, investment returns and cash flows into the Fund, the estimated funding level fell by approximately 7% over the year to 31 March 2015, to c. 78%.
- This was largely driven by the actuarial valuation interest rate decreasing, increasing the value placed on the liabilities (dropping from 5.1% p.a. to 3.9% p.a. as a result of falling gilt yields), offset slightly by lower inflation expectations.
- Over the coming year, the Fund will be undertaking work to review the alignment of its assets (particularly the Stabilising Assets) and movements in liabilities.
- At the valuation date, 31 March 2013, the Scheme was 78% funded; as at 31 March 2015 the funding level was broadly unchanged, although the size of the deficit had grown from £876m to c. £1.1bn.

Consideration of Funding Level
Fund performance relative to estimated liabilities



- The Fund's assets, scaled to take into account the estimated funding level, produced an absolute return of 10.9%, over the year.
- However, the Fund's estimated liabilities increased by 23.9% (primarily due to a fall in the discount rate, offset to some extent by a decrease in the inflation assumption used to value inflation-linked liabilities).
- Over the year, the "cashflow effect" from contributions was a positive 1.8%. The significant 1.9% impact in Q2 2014 represents several employing bodies paying their deficit payments in advance.
- Overall, the combined effect has led to a decrease in the estimated funding level to 78% (from c. 84% at 31 March 2014).

Section 3

Fund Valuations – 31 March 2015

Fund Valuations
Valuation by asset class – 31 March 2015

Asset Allocation

Asset Class	31/03/2014 (£'000)	31/03/2015 (£'000)	31/03/2014 (%)	31/03/2015 (%)	Target Strategic Benchmark (%)	Ranges (%)	Difference (%)
Developed Market Equities	1,567,935	1,769,396	47.1	46.2	40.0	35 - 45	+6.2
Emerging Market Equities	311,776	351,961	9.4	9.2	10.0	5 - 15	-0.8
Diversified Growth Funds	314,340	368,177	9.4	9.6	10.0	5 - 15	-0.4
Fund of Hedge Funds	162,986	162,792	4.9	4.3	5.0	0 - 7.5	-0.7
Property	260,987	306,177	7.8	8.0	10.0	5 - 15	-2.0
Infrastructure	-	-	-	-	5.0	0 - 7.5	-5.0
Bonds	640,599	798,547	19.2	20.9	20.0	15 - 35	+0.9
Cash (including currency instruments)	71,739	71,606	2.2	1.9	-	0 - 5	+1.9
Total	**3,330,362**	**3,828,656**	**100.0**	**100.0**	**100.0**		**0.0**

Source: WM Performance Services, managers. Green numbers indicate the allocation is within tolerance ranges, whilst red numbers indicate the allocation is outside of tolerance ranges. May not sum due to rounding.

Invested assets increased over the year by c £500m.

Over the quarter, the developed market equity allocation has been reduced but remains over weight and outside of tolerance ranges; this overweight will be used to fund drawdowns for the infrastructure allocation over the coming year. The investment in Standard Life GARS has brought the DGF allocation back close to the target weight.

Fund Valuations
Valuation by manager – 31 March 2015

Manager Allocation					
Manager	**Asset Class**	**31/03/2014 (£'000)**	**31/03/2015 (£'000)**	**31/03/2014 (%)**	**31/03/2015 (%)**
BlackRock	Passive Multi-Asset	1,026,945	1,216,557	30.9	31.8
Jupiter	UK Equities	160,880	175,562	4.8	4.6
TT International	UK Equities	185,267	194,929	5.6	5.1
Schroder	Global Equities	214,480	256,314	6.4	6.7
Genesis	Emerging Market Equities	145,088	160,236	4.4	4.2
Unigestion	Emerging Market Equities	166,687	191,725	5.0	5.0
Invesco	Global ex-UK Equities	239,795	291,423	7.2	7.6
SSgA	Europe ex UK & Pacific inc. Japan Equities	107,146	124,517	3.2	3.3
Record Currency Management	Dynamic Currency Hedging	12,044	0	0.4	0.0
Record Currency Management	Overseas Equities (to fund currency hedge)	15,988	20,608	0.5	0.5
Pyrford	DGF	104,542	124,700	3.1	3.3
Barings	DGF	209,798	-	6.3	-

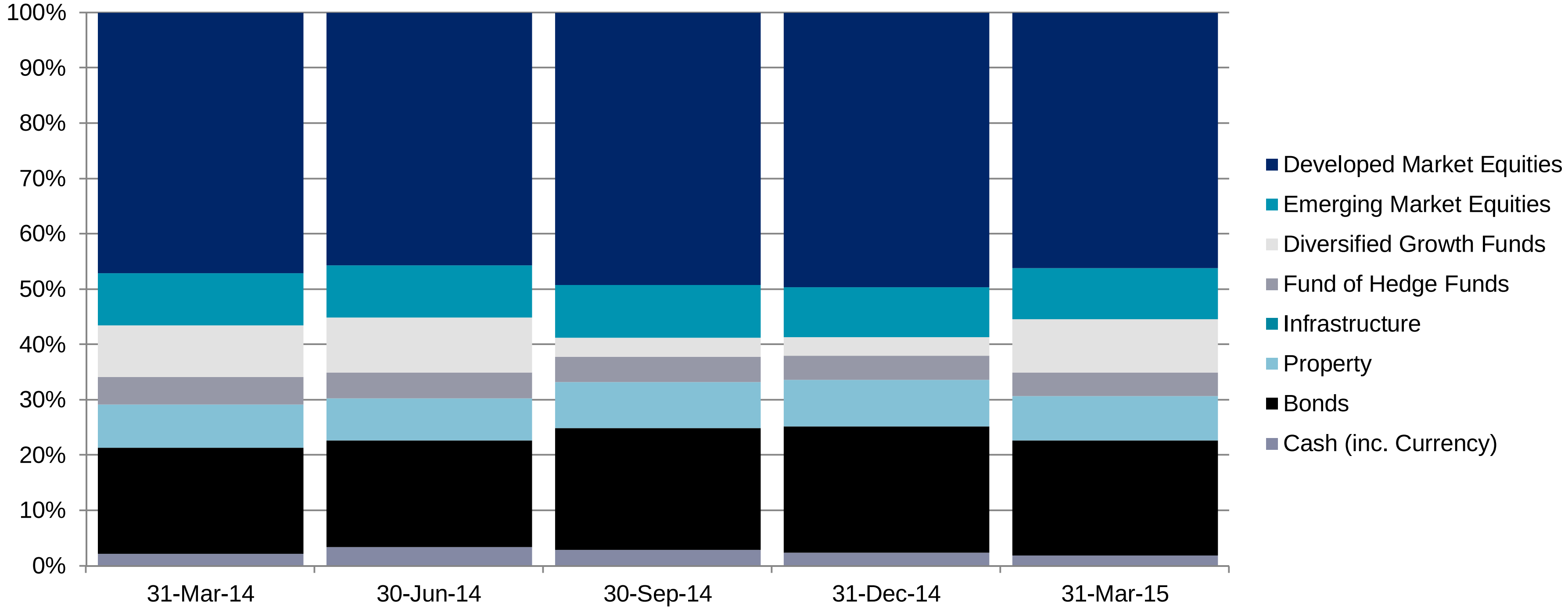
Source: WM Services, Avon. Totals may not sum due to rounding. *estimated holding at 31 March 2015.

Fund Valuations
Valuation by manager – 31 March 2015

Manager Allocation					
Manager	**Asset Class**	**31/03/2014 (£'000)**	**31/03/2015 (£'000)**	**31/03/2014 (%)**	**31/03/2015 (%)**
Standard Life	DGF	-	243,477	-	6.4
MAN	Fund of Hedge Funds	1,115	549*	0.0	0.0
Signet	Fund of Hedge Funds	66,155	63,441	2.0	1.7
Stenham	Fund of Hedge Funds	37,654	39,661	1.1	1.0
Gottex	Fund of Hedge Funds	58,062	59,141	1.7	1.5
Schroder	UK Property	150,249	177,723	4.5	4.6
Partners	Property	112,058	136,985*	3.4	3.6
RLAM	Corporate Bonds	249,851	308,883	7.5	8.1
BlackRock (property fund)	Equities, Futures, Bonds, Cash (held for property inv)	45,643	0	1.4	0.0
Internal Cash	Cash	20,915	42,224	0.6	1.1
Total		**3,330,362**	**3,828,656**	**100.0**	**100.0**

Source: WM Services, Avon. Totals may not sum due to rounding. *estimated holding at 31 March 2015.

Commentary on change in asset allocation over year



The asset allocation remained broadly unchanged over the year, with the exception of the disinvestment from Barings in Q3 2014 following the departure of the fund's key managers. The proceeds from this disinvestment were held in bonds and developed market equities in BlackRock's multi-asset portfolio (to broadly reflect the underlying Barings allocations), resulting in the increased allocation to these asset classes and lower exposure to DGF seen at 30 September 2014 and 31 December 2014.

In mid February 2015, £240m was invested in the Standard Life GARS (a replacement DGF vehicle), taken from the cash holdings and the BlackRock multi-asset portfolio, returning the DGF holdings to near the strategic benchmark.

Equity holdings remain overweight, in the anticipation that the Infrastructure mandate will be funded from equities.

Section 4

Market Background

Market Background
Index Performance over the year to 31 March 2015

Equity Markets– strong returns

Global equity markets continued to post positive performance over the year, returning 19.2% in sterling and 14.3% in local currency terms.

Despite robust economic growth, UK equities rose by 6.6% over the year to 31 March 2015, lagging the wider global equity markets.

Equity returns were strongest in the US, at 26.4% for the year. Emerging market assets underperformed their developed counterparts, with equities rising by 16.3%, as falling commodity prices and the rising US dollar affected a number of countries in this region significantly. Japanese equities performed strongly, returning 27.1% in sterling terms and 31.8% in local currency terms, driven by some initial signs of economic recovery following a technical recession triggered by the value-added tax hike in 2014. European equities were weaker, returning 7.5% in sterling and 19.3% in local currency terms (as the long awaited ECB announcement regarding euro-zone quantitative easing surpassed market expectations, which caused the euro to depreciate in Q1 2015).

Bond Markets– strong returns

Bond market yields fell further over the second half of the year, particularly at the longer end of the yield curve. The yield for the FTSE Gilts All Stocks index fell over the year from 3.0% p.a. at 31 March 2014 to 2.0% p.a. at 31 March 2015. As a result, returns on UK Government bonds as measured by the FTSE Gilts All Stocks Index were strong at 13.9%, while long dated issues as measured by the corresponding Over 15 Year Index recorded growth of 27.0%.

Real yields also fell over the year, with the FTSE All Stocks Index Linked Gilts index returning 18.6% andthe corresponding over 15 year index also exhibiting a positive return of 28.1%.

Global credit returned -1.1% in local currency terms, but +11.1% in sterling terms on the back of a weakening pound relative to the dollar.

In a broader risk-on environment, credit spreads tightened over the year, which in combination with falling gilt yields resulted in a total return of 13.2% for the UK corporate bonds over the year to 31 March 2015.

Currency Markets – mixed performance from sterling

Over the 12 month period to 31 March 2015, sterling fell 11.0% against the US Dollar from $1.667 to $1.485. Sterling appreciated 3.7% against the Yen from ¥171.69 to ¥178.03, and also appreciated against the Euro by 14.3% from €1.21 to €1.38 over the same period.

Commodity Markets – material falls

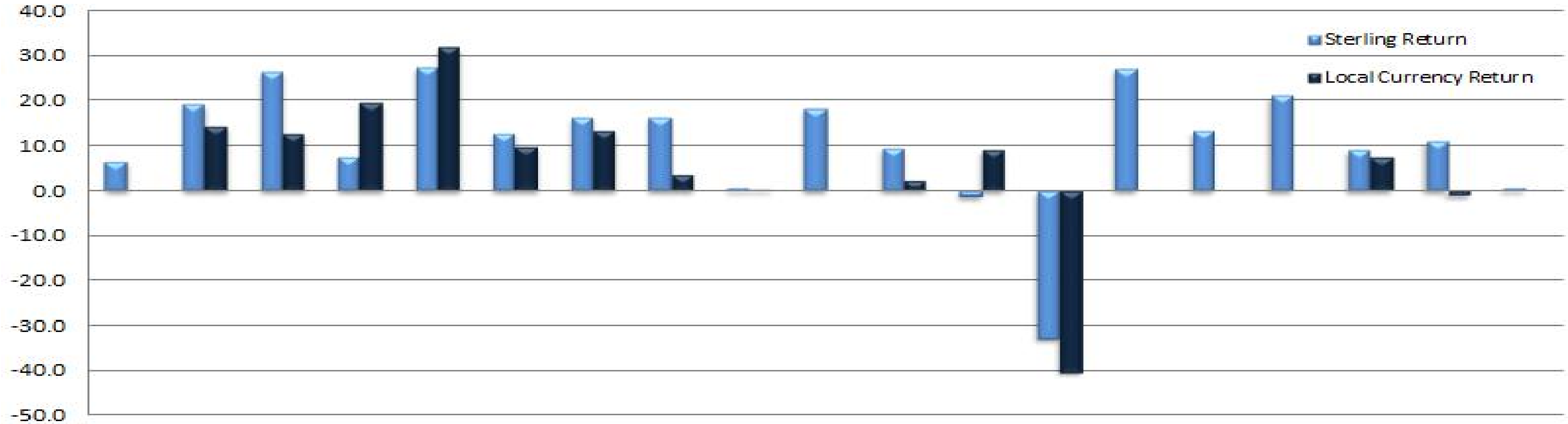
The price of Brent Crude fell significantly (by 49.2%) from $107.31 to $54.56 per barrel over the one year period to 31 March 2015. Over the same period, the price of Gold also depreciated by 7.9% from $1289.28 per troy ounce to $1187.60.

The S&P GSCI Commodity Spot Index fell by 33% over the one year period to 31 March 2015 in sterling terms.

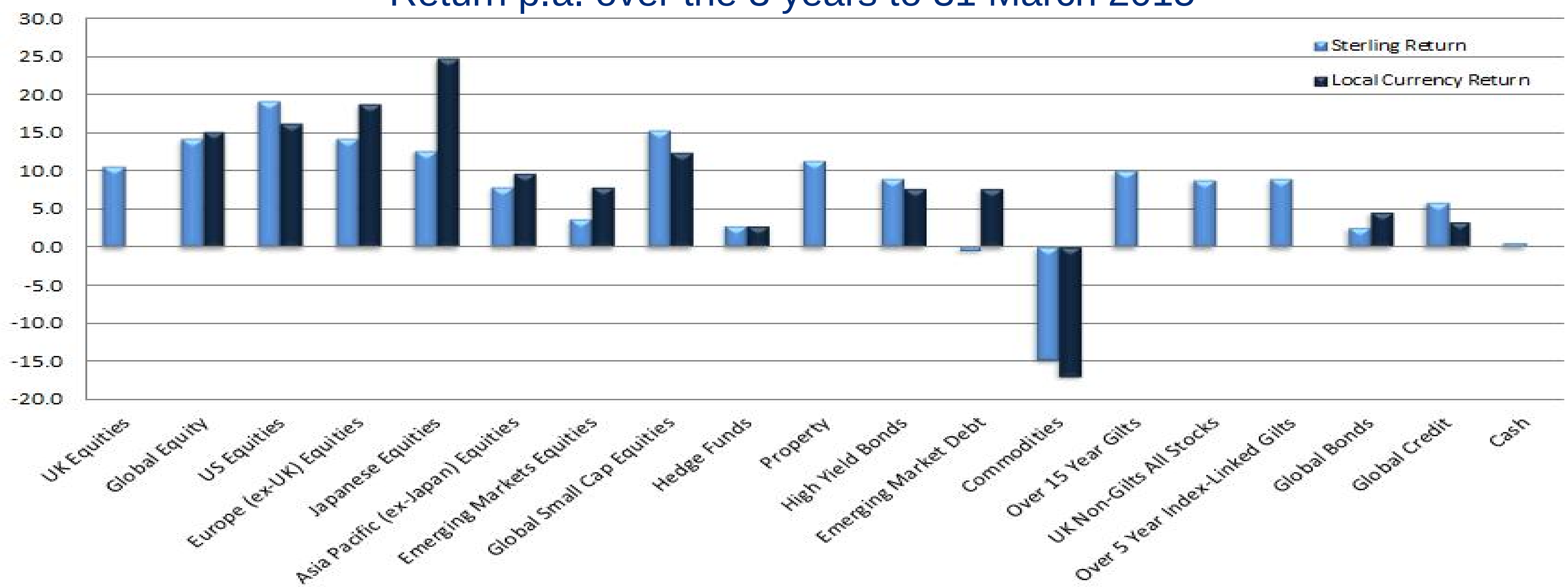
Source: Thomson Reuters Datastream.

Market Background
Index Performance

Return over the 12 months to 31 March 2015



Return p.a. over the 3 years to 31 March 2015

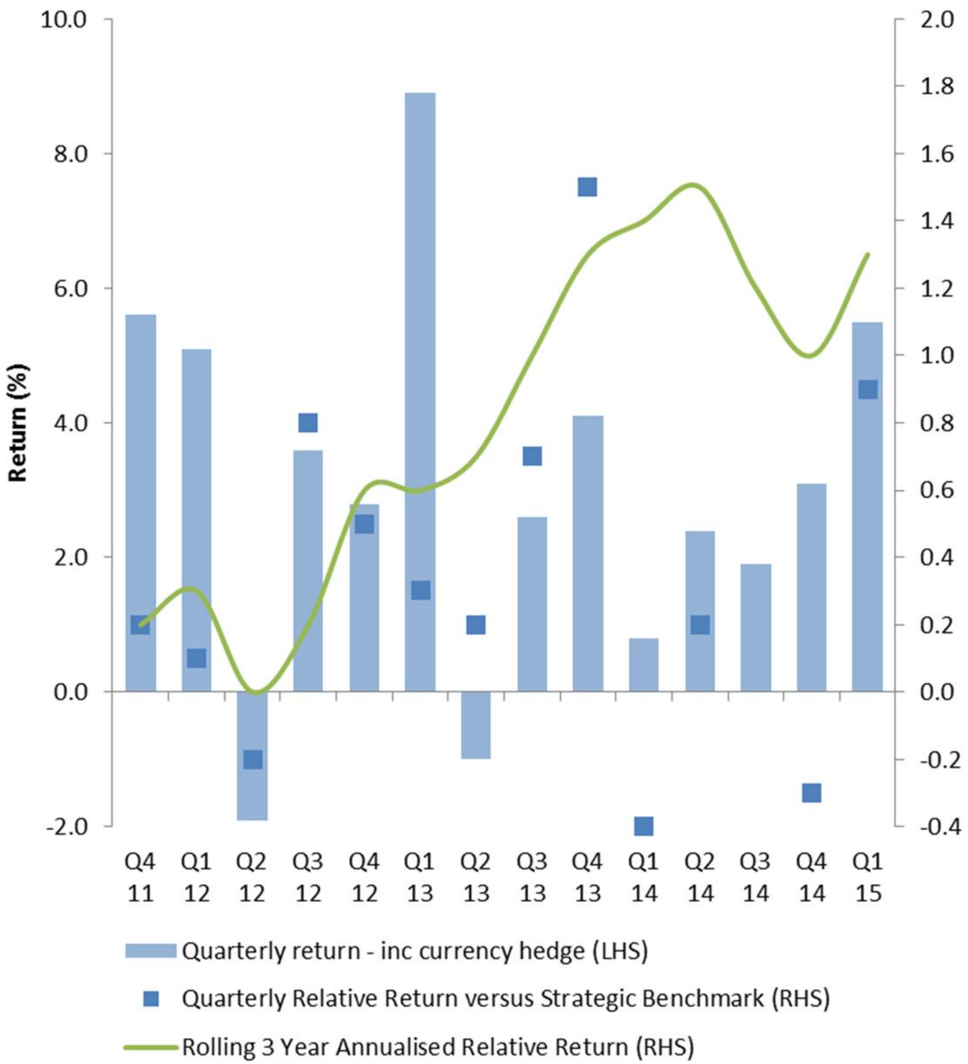


Source: Thomson Reuters Datastream.

Section 5

Performance Summary

Performance summary
Total Fund Performance



	3 months (%)	1 year (%)	3 years (% p.a.)
Total Fund (inc currency hedge)	5.5	13.5	11.2
Total Fund (ex currency hedge)	5.4	13.3	11.0
Strategic Benchmark (no currency hedge)	4.6	13.2	9.9
Relative (inc currency hedge)	**+0.9**	**+0.3**	**+1.3**

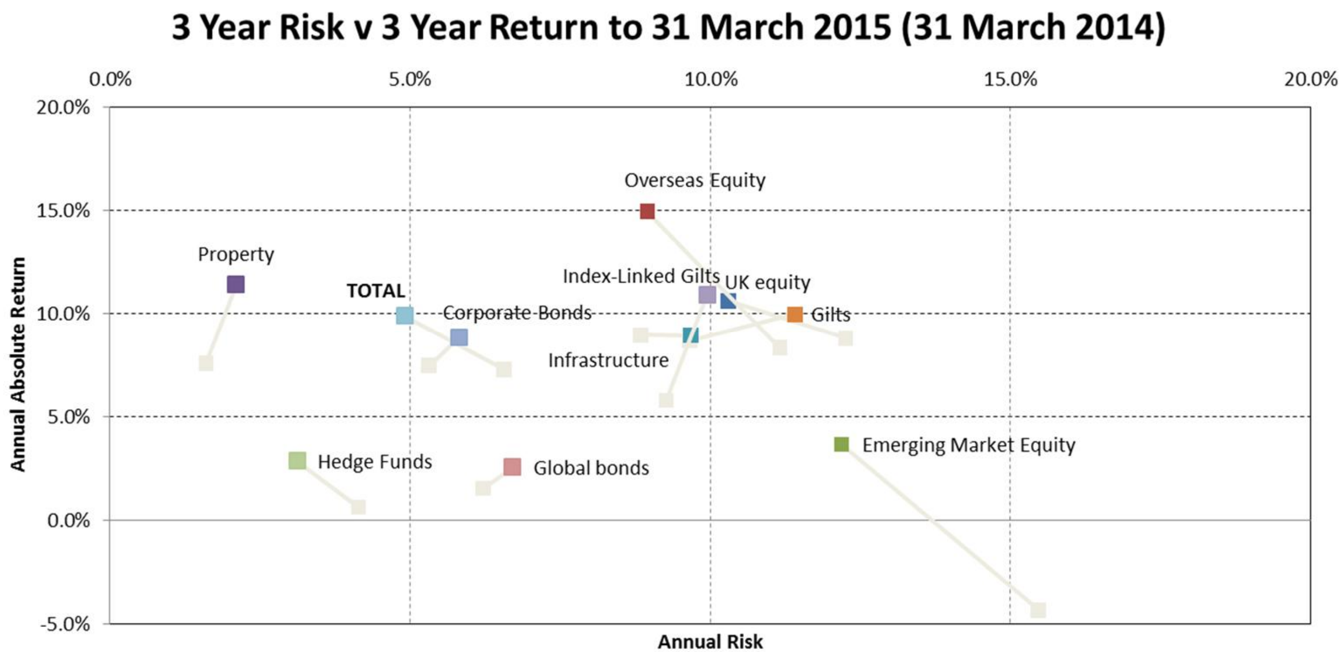
- Over the year to 31 March 2015, the Fund outperformed its Strategic Benchmark by 0.3% when including the currency hedge, and by 0.1% when not including the currency hedge.
- The largest component of the year's outperformance was the overweight position in overseas developed equities (which outperformed the Fund's returns as a whole), and the outperformance of the multi-asset mandates relative to their benchmarks.
- The Fund has also outperformed the Strategic Benchmark over the three year period, by 1.3% p.a. including the currency hedging returns.
- The last year's outperformance was marginally lower than that for the year to 31 March 2012, and as a result the rolling three year outperformance has dropped slightly from 1.4% p.a. to 1.3% p.a.

Performance summary
Index Performance versus strategic benchmark

Asset Class	Weight in Strategic Benchmark (From October 2013)[1] (%)	Index returns 1 year (%)	Contribution to total benchmark 1 year (%)	Index returns 3 years (% p.a.)	Contribution to total benchmark 3 years (% p.a.)	Assumed strategic return: Return (% p.a.)	Assumed strategic return: Contribution[2] (% p.a.)
UK Equities	**15.0**	6.6	1.0	**10.6**	1.8	**8.25**	0.5
Overseas Equities	**25.0**	20.3	5.1	**15.5**	4.7	**8.25**	2.1
Emerging Market Equities	**10.0**	12.8	1.3	**3.2**	0.4	**8.75**	-0.3
Diversified Growth Funds	**10.0**	4.6	0.5	**4.6**	0.2	**4.6**	-0.1
UK Government Bonds	**3.0**	26.9	0.8	**10.0**	0.4	**4.5**	0.1
UK Corporate Bonds	**8.0**	13.1	1.1	**8.8**	0.6	**5.5**	0.3
Index Linked Gilts	**6.0**	21.0	1.3	**8.9**	0.6	**4.25**	0.3
Overseas Fixed Interest	**3.0**	7.6	0.2	**1.0**	0.0	**5.5**	-0.1
Fund of Hedge Funds	**10.0**	4.6	0.5	**4.6**	0.3	**6.0**	-0.3
Property	**10.0**	16.6	1.7	**9.4**	1.0	**7.0**	0.3
Total Fund	**100.0**		**13.2**		**9.9**	**7.1**	**+2.8**

Source: WM and Mercer estimates. May not sum due to rounding.
1. Allocations used by WM to calculate the total strategic benchmark return BEFORE the agreed investment in infrastructure.
2. Contribution to total difference between strategic benchmark return over last three years (9.9% p.a.) and overall assumed strategic return (7.1% p.a.) – weighted by strategic benchmark

Performance summary
Risk Return Analysis



This chart shows the 3 year absolute returns against three year volatility (based on monthly data in sterling terms), to the end of March 2015, for each of the broad underlying asset benchmarks (using the indices set out in the Appendix), along with the total Fund strategic benchmark (using the benchmark indices and allocations from WM Services). We also show the positions as at 31 March 2014, in grey.

Comments

- *The three-year period to 31 March 2015 excludes the year to 31 March 2012 which was included in the previous year's analysis.*
- *The most significant changes seen over the period were the fall in risk and increased returns seen for overseas equities, as 2014/15 was significantly less volatile than the year to 31 March 2012. Three year returns for UK equities also rose and volatility fell, albeit more modestly.*
- *Three year returns for bonds also rose marginally given the fall in yields in late 2014 / early 2015, while backward-looking risk measures rose for gilts in light of the recent volatility.*

Active investment manager contribution – year to 31 March 2015

Asset Class	Weight in Strategic Benchmark		Average overweight position	Fund return	Index return	Asset allocation impact	Active management's impact
	Start (%)	End (%)	(%)	(%)	(%)	(%)	(%)
UK Equities	15.0	15.0	1.1	6.5	6.6	-0.1	-
Overseas Equities	25.0	25.0	5.5	18.6	20.3	+0.4	-0.4
Emerging Market Equities	10.0	10.0	-0.7	12.9	12.8	-	-
Diversified Growth Funds	10.0	10.0	-0.4	9.4	4.6	+0.3	+0.2
UK Government Bonds	3.0	3.0	-0.2	26.9	26.9	-	-
UK Corporate Bonds	8.0	8.0	0.4	13.8	13.1	-	+0.1
Index Linked Gilts	6.0	6.0	0.0	21.1	21.0	-	-
Overseas Fixed Interest	3.0	3.0	-0.4	7.5	7.6	-	-
Fund of Hedge Funds	10.0	10.0	-5.5	0.2	4.6	+0.4	-0.2
Property	10.0	10.0	-1.3	13.4	16.6	-0.3	-0.2
Total Fund	**100.0**	**100.0**		**13.3**	**13.2**	**0.7**	**-0.6**

Source: WM and Mercer estimates. May not sum due to rounding.
Average overweight position taken as the average of the beginning and end of year weights.

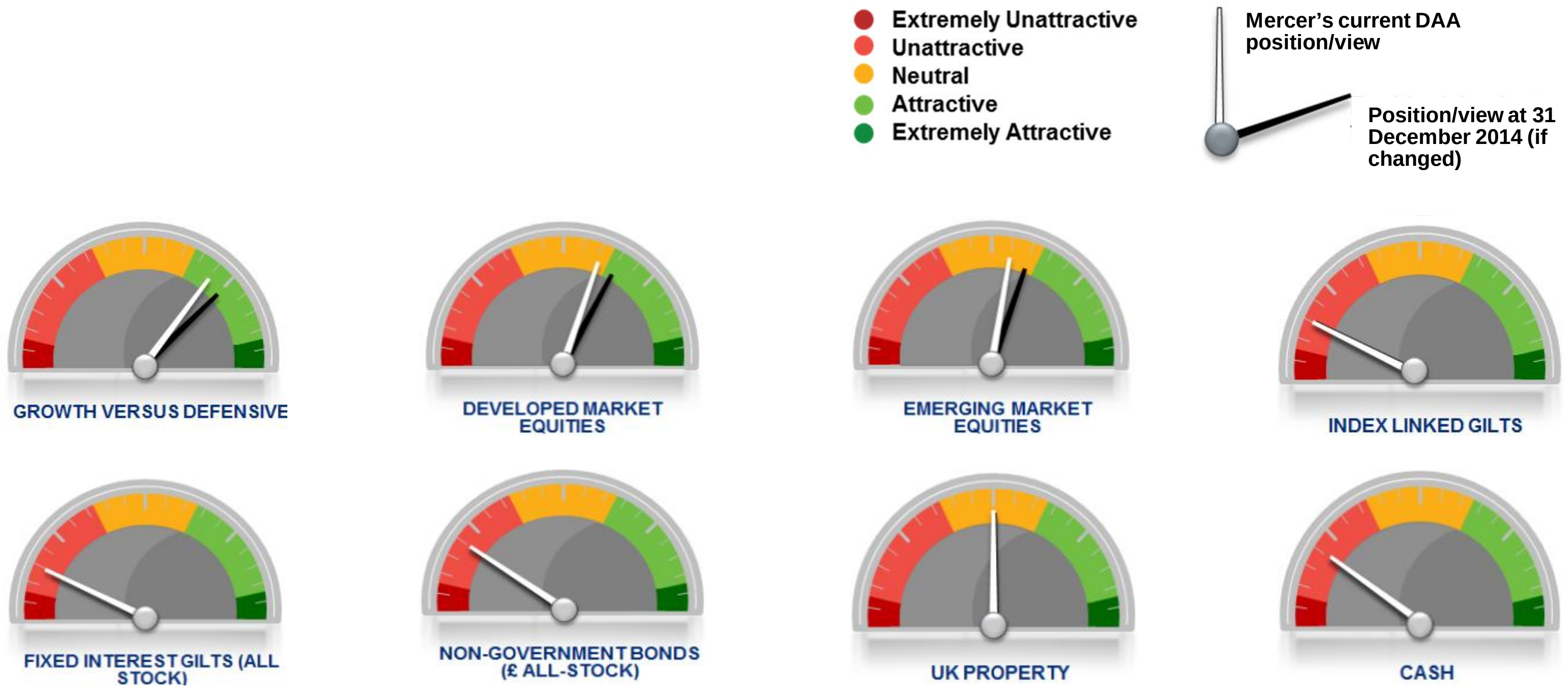
Manager monitoring

Manager Performance – returns relative to benchmark (to 31 March 2015)

Manager / fund	1 year (%)	3 years (% p.a.)	3 year versus performance target
BlackRock Multi - Asset	0.0	0.1	Target met
Jupiter	2.0	4.1	Target met
TT International	-1.6	2.5	Target not met
Schroder Equity	0.0	0.0	Target not met
Genesis	-2.8	1.2	Target met
Unigestion	2.2	NA	NA
Invesco	1.2	1.2	Target met
SSgA Europe	0.6	1.5	Target met
SsgA Pacific	1.9	1.6	Target met
Pyrford	1.2	NA	NA
Standard Life	NA	NA	NA
Signet	-7.7	-4.1	Target not met
Stenham	1.7	2.4	Target met
Gottex	-1.8	0.2	Target met
Schroder Property	0.7	1.6	Target met
Partners Property	-10.1	-3.1	Target not met
RLAM	0.2	2.2	Target met

Source: WM Services, Avon.
Returns in blue text exceeded their respective benchmarks, those in red underperformed, and black text shows performance in line with benchmark.
Individual manager performance can be found in Appendix 1.

Forward looking return expectations – 31 March 2015



These charts summarise Mercer's views on the medium term outlook for returns from the key asset classes; by medium term we mean one to three years. These views are relevant for reflecting medium term market views in determining appropriate asset allocation. We do not expect investors to make frequent tactical changes to their asset allocation based upon these views. These are also based from the view of an absolute return investor, and so do not take into account pension scheme liabilities.

Forward looking return expectations – changes over the last year

Asset Class	April 2014	July 2014	Oct 2014	Jan 2015	April 2015
Fixed Interest Gilts	Unattractive	Unattractive	Unattractive	Unattractive	Unattractive
Index-Linked Gilts	Unattractive	Unattractive	Unattractive	Unattractive	Unattractive
Non-Government Bonds (£ All-Stocks)	Unattractive	Unattractive	Unattractive	Unattractive	Unattractive
Global Equities	Attractive	Attractive	Attractive	Attractive	**Neutral**
Emerging Market Equities	Attractive	Attractive	Attractive	**Neutral**	Neutral
UK Property	Attractive	Attractive	**Neutral**	Neutral	Neutral
UK Cash	Unattractive	Unattractive	Unattractive	Unattractive	Unattractive

Valuation Scale: Extremely Attractive → Attractive → Neutral → Unattractive → Extremely Unattractive, Bold items represent views that have changed from the previous meeting

Appendix 1

Manager Monitoring

Manager monitoring
UK Equities

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance*	Fund	B'mark	Relative	Target	Contribution to outperformance*
Jupiter	8.6	6.6	+2.0	+0.09	14.7	10.6	+4.1	+2	+0.17
TT International	5.0	6.6	-1.6	-0.09	13.1	10.6	+2.5	+3	+0.12

Source: WM Services / Mercer estimates. "Contribution to outperformance" is the annualised impact on total return of the individual managers' performance relative to their benchmark over the periods measured, and provides an indication of the relative impact of manager out- or under-performance.

Market Commentary

- UK Equities rose over the year, returning 6.6%, driven by positive economic news. This lagged global markets which returned 19.2%, driven by strong US equities which returned 26.4% in sterling terms.

Performance Commentary

- Jupiter have outperformed over the one and three year periods. Tracking error has stayed between c3.6% and 3.8% over the year, with overall volatility consistently below that of the benchmark index. While UK equities returned 6.6% over the year, over the same period the median UK active manager in Mercer's universe outperformed the FTSE All-Share by 1.2%, placing Jupiter's performance above median as well as above benchmark.

- Holdings remain noticeably different from the benchmark, due in large part to its Socially Responsible Investment objectives – having a significant underweight to large cap stocks and overweight to midcap stocks.

- TT's unconstrained mandate underperformed over the year but outperformed over the three year period, with strong stock selection being a significant driver of returns. The portfolio holds a significant overweight position in Consumer Services (21.3% vs 12.0% in the benchmark) and smaller over weights in Consumer Goods, Healthcare and Telecoms.

Manager monitoring
Developed Global Equities

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
Invesco	21.5	20.3	+1.2	+0.09	16.7	15.5	+1.2	+0.5	+0.08
SSgA Europe	7.4	6.8	+0.6	+0.01	14.9	13.4	+1.5	+0.5	+0.01
SSgA Pacific	21.3	19.4	+1.9	+0.03	11.9	10.3	+1.6	+0.5	+0.03
Schroder	19.0	19.0	0.0	+0.01	14.1	14.1	0.0	+4.0	+0.01

Source: WM Services / Mercer estimates

Market Commentary

- Global equities were strong over the year, producing a 19.2% return. This was largely driven by strong returns in the US (26.4%) and Japan (27.1%).

Performance Commentary

- All managers at least achieved their benchmarks over the one and three year periods, although Schroder have significantly lagged their target of +4% p.a. As a result, all managers contributed positively to outperformance over the year and three-year periods.
- Invesco's tracking error remains small at 1.5% p.a. since inception, while sector and country allocations remain relatively close to benchmark weightings (as would be expected for an enhanced indexation product), with all within +/- 1.2% at 31 March 2015.
- Schroder's active share (the percentage of stock holdings in a manager's portfolio that differ from the benchmark index) remains high at around 90%, but while performance from stock selection and asset allocation has been positive over the last few months, longer term performance remains relatively disappointing. The Investment Panel has been actively monitoring changes made by Schroder to improve performance.

Manager monitoring
Emerging Market Equities

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
Genesis	10.4	13.2	-2.8	-0.10	4.4	3.2	+1.2	-	+0.07
Unigestion	15.0	12.8	+2.2	+0.10	N/A	N/A	N/A	+2-4	N/A

Source: WM Services / Mercer estimates.

Market Commentary

- Emerging market assets underperformed their developed market counterparts, with equities rising by 16.3% (FTSE All World Emerging), against 19.4% return from the FTSE All World Developed, as falling commodity prices and the rising US dollar affected a number of countries in this region significantly.

Performance Commentary

- Unigestion have outperformed their benchmark over the year. Over the period since inception (in January 2014), they have returned 12.9% p.a. against a benchmark return of 12.1% p.a. They have achieved this with lower volatility than the benchmark (11.0% p.a. vs 12.6% p.a.). The largest regional weighting of the portfolio is in China (23%) and the vast majority of holdings (89.7%) are in mega- or large-cap stocks.
- Genesis have underperformed by 2.8% over the year, producing a negative contribution to overall Fund performance. This was largely due to underperformance in Q1 2015 (-2.25%), largely down to overweight positions in mining and oil companies (with a long-term overweight position to South Africa), and an underweight allocation to China (which performed well).
- However, over three years they have outperformed the benchmark by 1.2% p.a. and contributed positively to performance.

Manager monitoring
Fund of Hedge Funds

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
Signet	-4.1	3.6	-7.7	-0.14	-0.5	3.6	-4.1	-	-0.08
Stenham	5.3	3.6	+1.7	+0.02	6.0	3.6	+2.4	-	+0.03
Gottex	1.8	3.6	-1.8	-0.03	3.8	3.6	+0.2	-	0.00

Source: WM Services / Mercer estimates

The Fund is in the process of divesting from all three managers listed above, with the allocation to be managed by JPMorgan in a bespoke fund of funds vehicle.

Market Commentary

- Fund of Hedge Funds have generally lagged equity markets over the year and three years, but looking ahead we would expect returns to be driven more by 'alpha' than beta, and hence stronger performance.

Performance Commentary

- Signet saw significant underperformance over the year, which led to a negative overall contribution to relative performance. This stemmed from the underperformance of their illiquid holdings in the Event Driven & Special Situations Fund (with the main holdings in the Global Fixed Income strategy returning +0.1% over the twelve month period).
- Stenham's long/short equity and global macro approach fared well over the year, outperforming its benchmark by 1.7% (outperforming their benchmark by 2.9% in Q1 2015 alone, as a result of strong equity returns across most markets and the US in particular).
- Gottex's market neutral approach underperformed over the year with poor returns in Q4 2014, but generated positive performance over the three-years to 31 March 2015.

Manager monitoring
Multi-Asset and DGF

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
BlackRock	15.9	15.9	0.0	-0.04	11.9	11.8	+0.1	-	+0.04
Pyrford	7.1	5.9	+1.2	+0.04	N/A	N/A	N/A	-	N/A

Source: WM Services / Mercer estimates.

Performance Commentary

- The passive multi-asset mandate managed by BlackRock continues to perform broadly in line with underlying indices (as expected).
- Pyrford outperformed their benchmark of RPI + 5% p.a. over the year to 31 March 2015, although performance lagged rising global equities (as would be expected). Over the period since inception (on 1 December 2013) they have underperformed their benchmark, returning 5.9% p.a. against a benchmark return of 6.6% p.a.
- The portfolio remains defensively positioned and the current equity weighting (at 30%) is the same as it was going into the financial crisis in 2008, and with 67% in short duration bonds (entirely held in UK, Canadian and US government stock).
- We have excluded Standard Life GARS from the above table given the limited investment period.

Manager monitoring
Corporate Bonds

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
RLAM	13.3	13.1	+0.2	+0.03	10.9	8.7	+2.2	+0.8	+0.14

Source: WM Services / Mercer estimates

Market Commentary

- In a broad risk-on environment, credit spreads tightened over the year, which in combination with falling gilt yields resulted in a total return of 13.3%* for UK corporate bonds
  *Noting that this is based on the return of the BofA Merrill Lynch Sterling Non Gilts All Stocks Index, which differs slightly from the iBoxx £ Non-Gilts All Maturities which RLAM is benchmarked against.

Performance Commentary

- RLAM have outperformed their benchmark over the one and three year periods by 0.2% and 2.2% respectively, significantly above their target of +0.8% p.a.
- Relative to the benchmark the portfolio has a shorter duration (7.6 years vs 8.2), a higher weighted average gross redemption yield (3.3% vs 2.6%) and a significantly more concentrated portfolio of stocks (at 273 vs 1,019).
- This reflects the positioning of the strategy, which has been consistently overweight BBB and BB bonds at the expense of AAA and AA, and with a sizable allocation to unrated bond (reflecting their longstanding view that higher yielding, lower rated bonds will outperformance investment grade credit).
- Looking ahead, our view is that prospective returns from UK corporate bonds will be more modest, as credit spreads have contracted; there is also the risk of inflation surprises and sudden increases to base rates. As a result, from an absolute return perspective we currently view UK corporate bonds as "unattractive".

Manager monitoring
Property

Manager / fund	1 Year(%)				3 years (% p.a.)				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
Schroder	17.3	16.6	+0.7	+0.04	11.0	9.4	+1.6	+1	+0.05
Partners	7.1	17.2	-10.1	-0.33	5.5	8.6	-3.1	-	-0.11

Market Commentary

- The UK property market was strong over the year, returning 16.6%. This comes with an improving UK economy as rental rates in commercial property increase, boosting property valuations.
- The global property market outperformed the UK market, returning 28.9% over the year in sterling terms. As with the UK, this performance is linked to the recovery of the global economy.

Performance Commentary

- Schroder outperformed their benchmark over the year and three-year periods to 31 March 2015, also outperforming their target of +1% p.a. over three years.
- Partners' drawdowns are made gradually over time, and the Fund is not yet fully invested. As a result of the volatile timing of cash flows for such investments, for example the initial costs of purchasing and developing properties, focus should be on longer term performance. Their IRR from inception to 31 December 2014 (the latest date currently available) at 9.3% p.a. is broadly in line with their target of 10% p.a.
- Schroder contributed 0.1% to total outperformance versus benchmark over the three-year period. Partners have detracted from performance over both and one and three-year periods (noting the above comment on the measurement of their returns).

Manager monitoring
Currency

Performance (Total Hedging Portfolio)	3 months (%)	1 year (%)	3 years (%)
Record Hedge	0.31	0.80	0.84
50% Illustrative Hedge	-1.22	-1.80	0.48
Relative	**+1.53**	**+2.60**	**+0.36**

Currency Hedging 12 Month Performance (£ terms)

Currency	Start Exposure (£)	End Exposure (£)	Currency Return (%)	50% Hedge Return (%)	Record Hedge Return (%)	Net Return (%)
USD	438,127,692	559,047,385	12.30%	-5.73%	-1.80%	10.38%
EUR	195,291,888	207,358,854	-12.49%	6.97%	8.83%	-4.51%
JPY	115,802,811	147,838,770	-3.56%	1.76%	-0.39%	-3.34%
Total	**749,222,392**	**914,245,009**	**3.82%**	**-1.80%**	**0.80%**	**4.74%**

Market Commentary

- Over the 12 month period to 31 March 2015, sterling fell 11.0% against the US Dollar from $1.667 to $1.485. Sterling appreciated 3.7% against the Yen from ¥171.69 to ¥178.03, and also appreciated against the Euro by 14.3% from €1.21 to €1.38 over the same period. Note that these are the inverse of the currency returns shown above.
- More recently, over the last quarter, the pound weakened against most major currencies as the Bank of England left interest rates unchanged, while indications from the US were that the Federal Reserve would be more inclined to increase rates (removing the label that it would be “patient” with any policy adjustments from its March statement).

Performance Commentary

- Over the year and three-years to 31 March 2015, Record out-performed a passive 50% hedge (one of the alternatives to dynamic currency hedging) at the total mandate level and also across US Dollar and Euro mandates given the relatively strong trends over the year, but underperformed the passive hedge on Yen.
- Record’s hedge added value in absolute returns on the Euro exposure over the year, but detracted with their positions in the US Dollar and Japanese Yen.
- The total size of the currency mandate has increased over the year, reflecting the growth in the value of the Fund’s equities.

Appendix 2

Summary of Mandates

Summary of Mandates

Manager	Mandate	Benchmark	Outperformance target (p.a.)
Jupiter Asset Management	UK Equities (Socially Responsible Investing)	FTSE All Share	+2%
TT International	UK Equities (Unconstrained)	FTSE All Share	+3-4%
Schroder	Global Equities (Unconstrained)	MSCI AC World Index Free	+4%
Genesis	Emerging Market Equities	MSCI EM IMI TR	-
Unigestion	Emerging Market Equities	MSCI EM NET TR	+2-4%
Invesco	Global ex-UK Equities (Enhanced Indexation)	MSCI World ex UK NDR	+0.5%
SSgA	Europe ex-UK Equities (Enhanced Indexation)	FTSE AW Europe ex UK	+0.5%
SSgA	Pacific inc. Japan Equities (Enhanced Indexation)	FTSE AW Dev Asia Pacific	+0.5%
Record	Active Currency Hedging	N/A	-
Pyrford	Diversified Growth Fund	RPI + 5% p.a.	-
Standard Life	Diversified Growth Fund	3 Month LIBOR +5% p.a.	-
Signet	Fund of Hedge Funds	3 Month LIBOR +3% p.a.	-
Stenham	Fund of Hedge Funds	3 Month LIBOR +3% p.a.	-
Gottex	Fund of Hedge Funds	3 Month LIBOR +3% p.a.	-
Schroder	UK Property	IPD UK Pooled	+1%
Partners	Overseas Property	IPD Global Pooled	+2%
Royal London Asset Management	UK Corporate Bonds	iBoxx £ Non-Gilts All Maturities	+0.8%
BlackRock	Passive Multi-Asset	In line with customised benchmarks using monthly mean fund weights	-
BlackRock	Overseas Property Account	Customised benchmarks using monthly mean fund weights	-
Cash	Internally Managed	7 Day LIBID	-

Appendix 3

Market Statistics Indices

Market statistics indices

Asset Class	Index
UK Equities	FTSE All-Share
Global Equity	FTSE All-World
Overseas Equities	FTSE World ex UK
US Equities	FTSE USA
Europe (ex-UK) Equities	FTSE W Europe ex UK
Japanese Equities	FTSE Japan
Asia Pacific (ex-Japan) Equities	FTSE W Asia Pacific ex Japan
Emerging Markets Equities	FTSE AW Emerging
Global Small Cap Equities	FTSE World Small Cap
Hedge Funds	HFRX Global Hedge Fund
High Yield Bonds	BofA Merrill Lynch Global High Yield
Emerging Market Debt	JP Morgan GBI EM Diversified Composite
Property	IPD UK Monthly Total Return: All Property
Commodities	S&P GSCI
Over 15 Year Gilts	FTA UK Gilts 15+ year
Sterling Non Gilts	BofA Merrill Lynch Sterling Non Gilts All Stocks
Over 5 Year Index-Linked Gilts	FTA UK Index Linked Gilts 5+ year
Global Bonds	BofA Merrill Lynch Global Broad Market
Global Credit	Barclays Capital Global Credit
Eurozone Government Bonds	BofA Merrill Lynch EMU Direct Government
Cash	BofA Merrill Lynch United Kingdom Sterling LIBOR 3 month constant maturity

These are the indices used in this report for market commentary; individual strategy returns are shown against their specific benchmarks.

Appendix 4

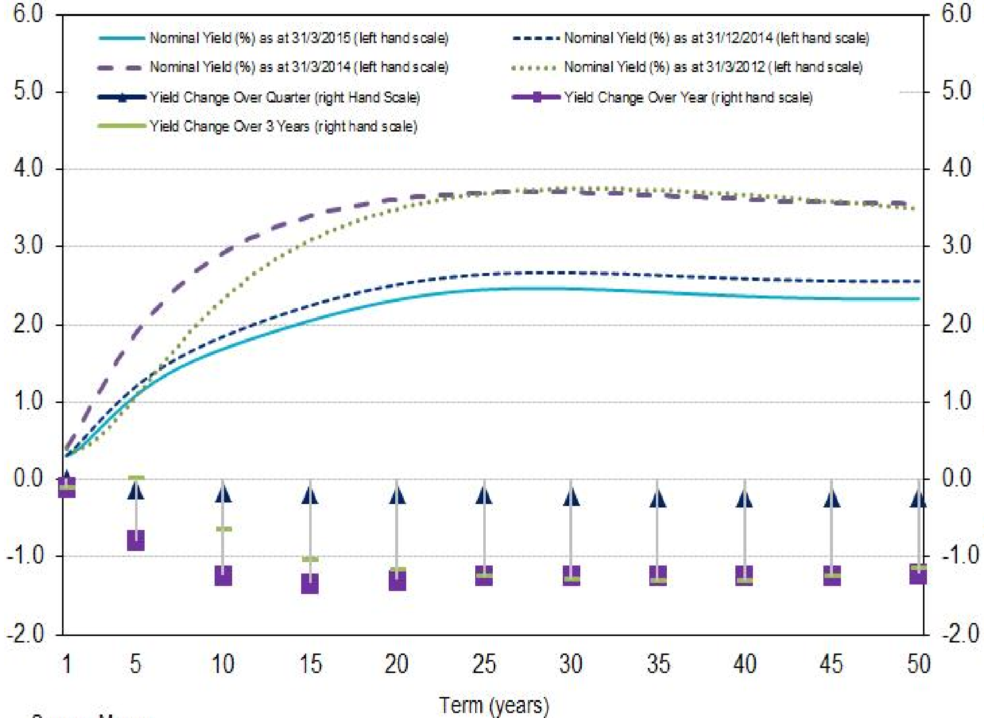
Changes in Yields

Changes in yields

Asset Class Yields (% p.a.)	31 March 2015	31 December 2014	31 March 2014	31 March 2012
UK Equities	3.33	3.37	3.41	3.45
Over 15 Year Gilts	2.23	2.42	3.43	3.26
Over 5 Year Index-Linked Gilts	-0.91	-0.75	-0.08	-0.09
Sterling Non Gilts	2.65	2.99	3.69	4.49

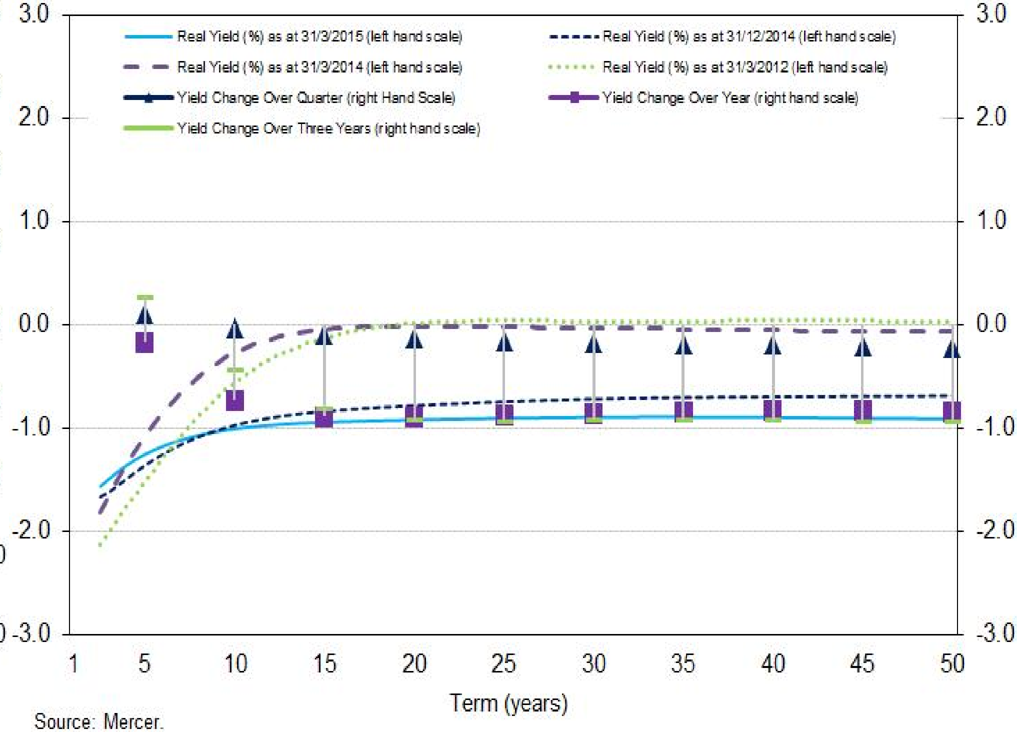
- Bond market yields fell significantly over the year, particularly at the longer end of the yield curve.
- Over 15 year gilt yields fell from 3.4% p.a. to 2.2% p.a. over the year, while the real yield curve also fell at most durations, with over 5 year index-linked gilt real yields falling from -0.1% to -0.9% p.a.
- Corporate bond yields (as shown by the Sterling non-gilt index) also fell over the year

Nominal yield curves.



Source: Mercer.

Real yield curves.



Source: Mercer.

MERCER