HEALTH WEALTH CAREER

AVON PENSION FUND

ANNUAL INVESTMENT REVIEW TO 31 MARCH 2017

JUNE 2017

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- The value of investments can go down as well as up and you may not get back the amount you have invested. In addition investments denominated in a foreign currency will fluctuate with the value of the currency.
- The valuation of investments in property based portfolios, including forestry, is generally a matter of a valuer's opinion, rather than fact.
- When there is no (or limited) recognised or secondary market, for example, but not limited to property, hedge funds, private equity, infrastructure, forestry, swap and other derivative based funds or portfolios it may be difficult for you to obtain reliable information about the value of the investments or deal in the investments.
- Where the investment is via a fund of funds the investment manager typically has to rely on the underlying managers for valuations of the interests in their funds.
- 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.

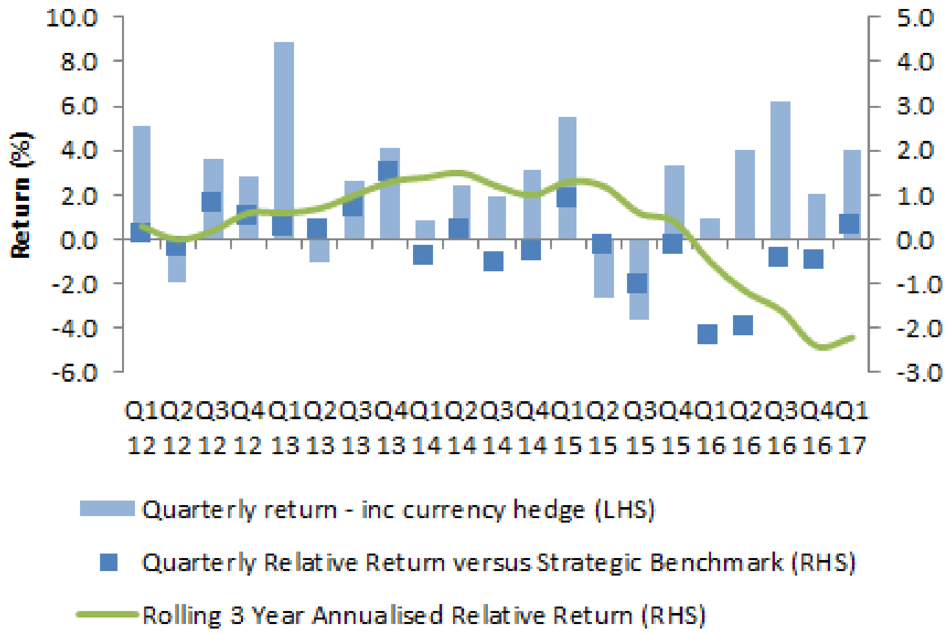
CONTENTS

SECTION 1
EXECUTIVE SUMMARY

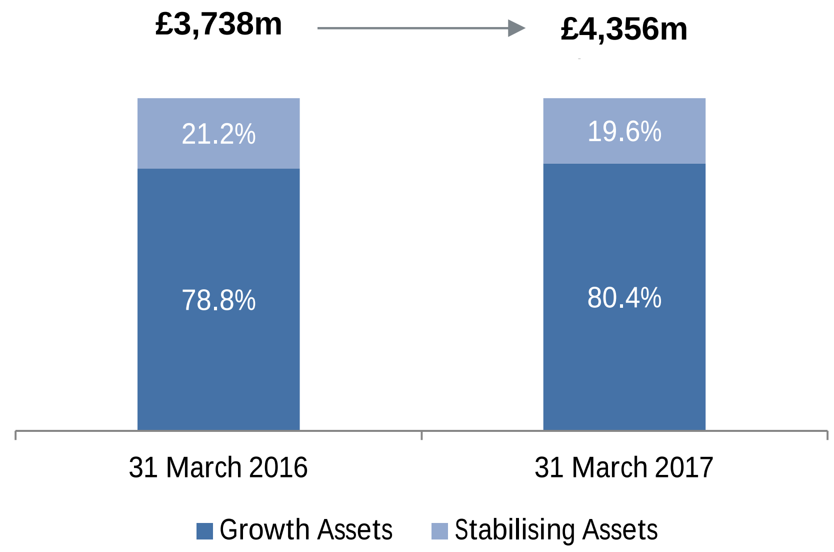
EXECUTIVE SUMMARY

	3 months (%)	1 year (%)	3 years (% p.a.)
Total Fund (inc currency hedge)	4.0	17.2	9.1
Total Fund (ex currency hedge)	3.8	20.2	10.8
Strategic Benchmark (no currency hedge)	3.7	20.1	11.3
Relative (inc currency hedge)	**+0.3**	**-2.9**	**-2.2**

Excess Return Chart



Asset Allocation



Commentary

Over the year total Fund assets (including currency hedging) increased from £3,738m (31 March 2016) to £4,356m.

This increase was primarily due to the strong positive performance from equities.

At a strategic level, the Fund was within the tolerance ranges in the Statement of Investment Principles for all asset classes at the end of the year.

The Fund marginally outperformed the unhedged strategic benchmark return (which excludes currency hedging) over the year. BlackRock and IFM were the main contributors to this performance whilst Unigestion, Standard Life and Jupiter were the main detractors.

When the currency hedge with Record is included, the Fund underperformed due to the significant depreciation of sterling over the year.

EXECUTIVE SUMMARY

This report has been prepared for the Committee of the Avon Pension Fund (“the Fund”), to assess the performance and risks of the investment managers of the Fund.

Funding level

- The estimated funding level increased by c.10% over the year, from 86% to 96% due to the positive return on the Fund’s assets exceeding the increase in the present value of the liabilities over the year.

Fund Performance

- The value of the Fund’s assets increased by £618m (16.5%) over the year, to £4,356m as at 31 March 2017. This increase was primarily due to the strong positive performance from equities, albeit bonds also performed strongly.

Strategy

- Global (developed) equity returns over the last three years were16.8% p.a., materially ahead of the assumed strategic return of 8.25% p.a. from the review in March 2013. We remain broadly neutral in our medium-term outlook for developed market equities (over the next one to three years). Accommodative monetary policy remains generally supportive of equity markets but uninspiring earnings growth and downward revisions to earnings estimates persist.

- The three-year return from emerging market equities has increased to 12.9% p.a. from -1.8% p.a. last year. It is therefore above the assumed strategic return (of 8.75% p.a.) as returns have been strong over the last year and fundamentals have improved. As with 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-year period remain significantly above the long-term assumed strategic returns as investor demand for gilts remains high. Fixed interest gilts returned 14.0% p.a. versus an assumed return of 4.5% p.a. and index-linked gilts returned 14.6% p.a. versus an assumed return of 4.25% p.a.

- UK corporate bonds returned 7.5% p.a. over the three-year period against an assumed strategic return of 5.5% p.a. The three-year UK property return of 11.2% p.a. remains substantially above the assumed return of 7% p.a.

Strategy (continued)

- Hedge fund returns remain below long-term averages and the strategic return of 6% p.a., having been affected by low cash rates. Active managers in general have struggled to generate meaningful returns in recent times.

Managers

- Absolute returns over the year to 31 March 2017 were strong. All mandates delivered positive absolute returns, with all overseas equities mandates returning over 20%, partly due to the significant weakening of sterling over 2016. However, a number of the active equity managers have underperformed their benchmarks over the year. This is partly due to value outperforming the wider market over the one-year period, which the Fund does not have a bias towards in its equity mandates. As such, relative performance should improve over periods where value suffers.

- Over the three-year period all mandates with a three-year track record produced positive absolute returns. A number of active funds underperformed their benchmarks over the period: Jupiter, Schroder global equities, Schroder property (over five years), Genesis, Unigestion, Pyrford and Partners (see comments on the measurement of Partners' performance later). TT, Invesco and Royal London failed to achieve their performance objectives but did outperform their respective benchmarks, net of fees. The SSgA mandates achieved their three-year performance objectives.

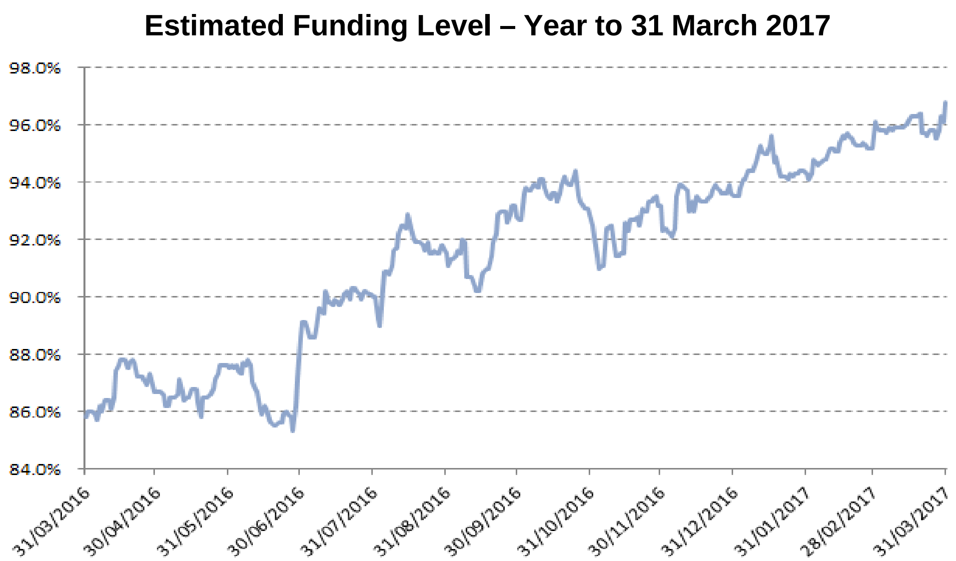
Key Points for Consideration

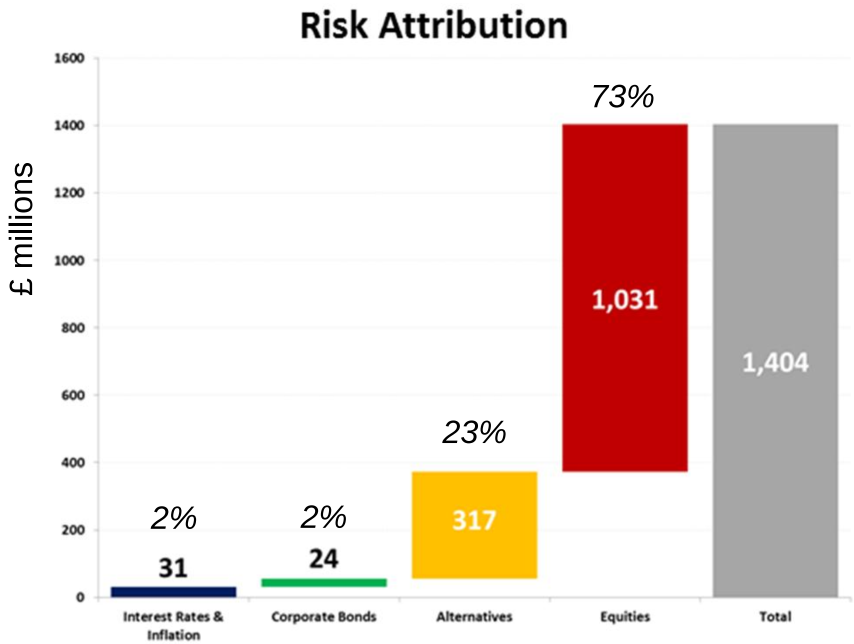
- Implementation of a liability risk management framework is in progress with BlackRock, which will include market-based triggers for increasing the level of hedging.

- An in-depth review of the Fund's broader investment strategy is also underway. The scope of this review includes the overall asset allocation, structure of the equity portfolio, possible approaches to equity risk management, future collateral management and currency hedging.

SECTION 2
CONSIDERATION OF FUNDING LEVEL

CONSIDERATION OF FUNDING LEVEL YEAR TO 31 MARCH 2017





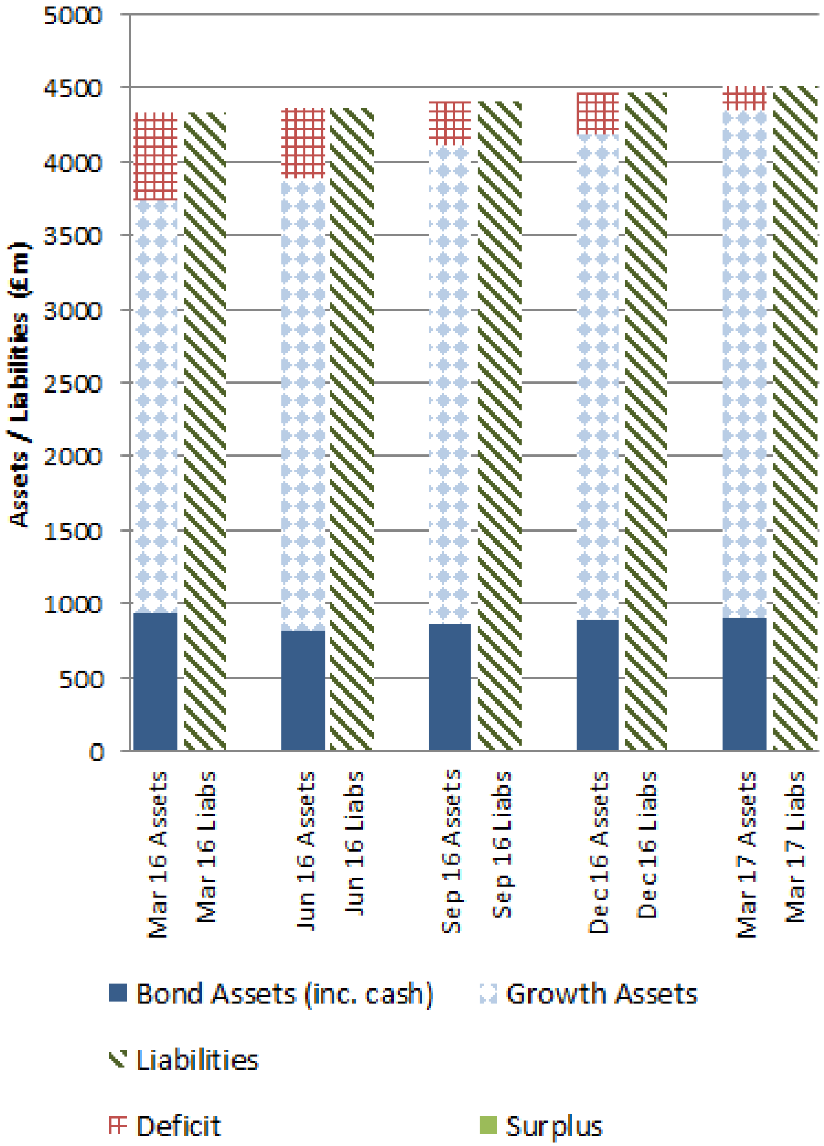
The charts above illustrate the estimated progression of the funding level (on the 2016 actuarial valuation basis) over the year to 31 March 2017 on the left hand side, and on the right the main risks the Fund is exposed to, again on the 2016 valuation basis, and also the size of these risks in the context 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, this is the impact on the deficit relative to our "best estimate" of what the deficit would be in one year's time. As at 31 March 2016, 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 **£1,404m** 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.** Equity risk dominates as the significant driver of volatility.

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.

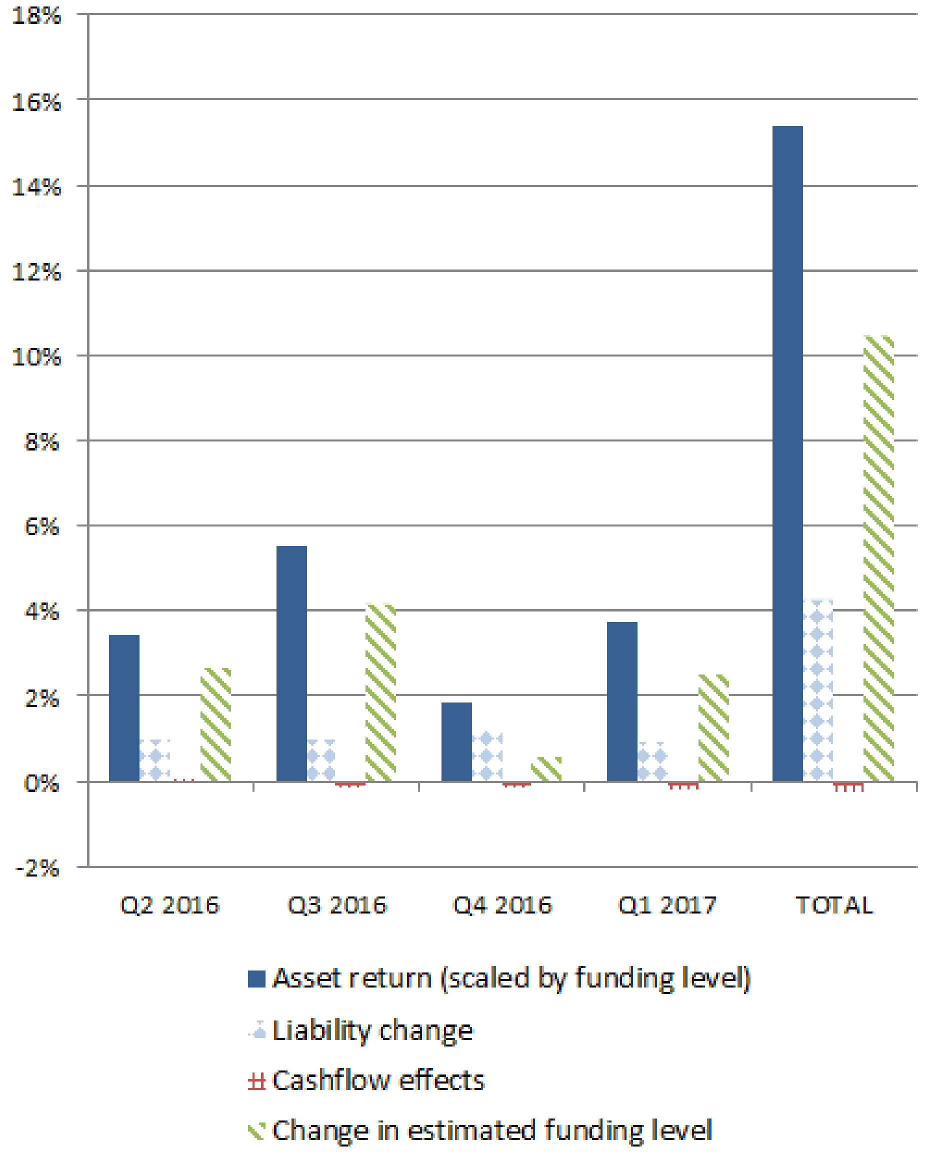
CONSIDERATION OF FUNDING LEVEL
ASSET ALLOCATION AND FUNDING LEVEL



- Based on financial markets, investment returns and cashflows into the Fund, the estimated funding level increased by c.10% over the year, all else being equal, from 86% to 96%. This was driven by a positive return on assets outweighing an increase in the present value of the liabilities.

- This is calculated using the new actuarial valuation as at 31 March 2016 and the “CPI plus” discount basis.

CONSIDERATION OF FUNDING LEVEL
FUND PERFORMANCE RELATIVE TO ESTIMATED LIABILITIES



- Over the 12 month period, the funding level has risen by c.10% due to the positive return on the Fund’s assets exceeding the increase in the present value of the liabilities over the year.
- The Fund’s assets returned 17.2% over the year, which, when allowing for the funding position, increased the funding level by 15.4%.

SECTION 3

FUND VALUATIONS

FUND VALUATIONS
VALUATION BY ASSET CLASS

Asset Allocation									
Asset Class	**31/03/2016 (£'000)**	**31/03/2017 (£'000)**	**31/03/2016 (%)**	**31/03/2017 (%)**	**Target Strategic Benchmark (%)**	**Ranges (%)**			**Difference (%)**
Developed Market Equities	1,544,963	1,776,492	41.3	40.8	40.0	35	-	45	+0.8
Emerging Market Equities	327,975	419,761	8.8	9.6	10.0	5	-	15	-0.4
Diversified Growth Funds	360,928	375,391	9.7	8.6	10.0	5	-	15	-1.4
Fund of Hedge Funds	192,394	228,648	5.1	5.2	5.0	0	-	7.5	+0.2
Property	362,097	380,488	9.7	8.7	10.0	5	-	15	-1.3
Infrastructure	-	256,003	-	5.9	5.0	0	-	7.5	+0.9
Bonds	792,149	852,657	21.2	19.6	20.0	15	-	35	-0.4
Cash (including currency instruments)	157,710	66,870	4.2	1.5	-	0	-	5	+1.5
Total	**3,738,216**	**4,356,309**	**100.0**	**100.0**	**100.0**				**0.0**

Source: BNY Mellon, Mercer. Green numbers indicate the allocation is within tolerance ranges, whilst red numbers indicate the allocation is outside of tolerance ranges.

- Invested assets increased over the year by £618m. This increase was primarily due to the strong positive performance from equities. At the end of the year, all asset classes were within the agreed tolerance ranges.

FUND VALUATIONS
VALUATION BY MANAGER

Manager Allocation					
Manager	**Asset Class**	**31/03/2016 (£'000)**	**31/03/2017 (£'000)**	**31/03/2016 (%)**	**31/03/2017 (%)**
BlackRock	Passive Multi-Asset	1,025,565	1,061,034	27.4	24.4
Jupiter	UK Equities	173,896	199,776	4.7	4.6
TT International	UK Equities	201,799	236,627	5.4	5.4
Schroder	Global Equities	253,892	337,292	6.8	7.7
Genesis	Emerging Market Equities	149,857	196,601	4.0	4.5
Unigestion	Emerging Market Equities	178,118	223,160	4.8	5.1
Invesco	Global ex-UK Equities	289,696	388,073	7.7	8.9
SSgA	Europe ex-UK & Pacific inc. Japan Equities	119,803	160,461	3.2	3.7
Pyrford	DGF	126,947	138,487	3.4	3.2
Standard Life	DGF	233,981	236,903	6.3	5.4

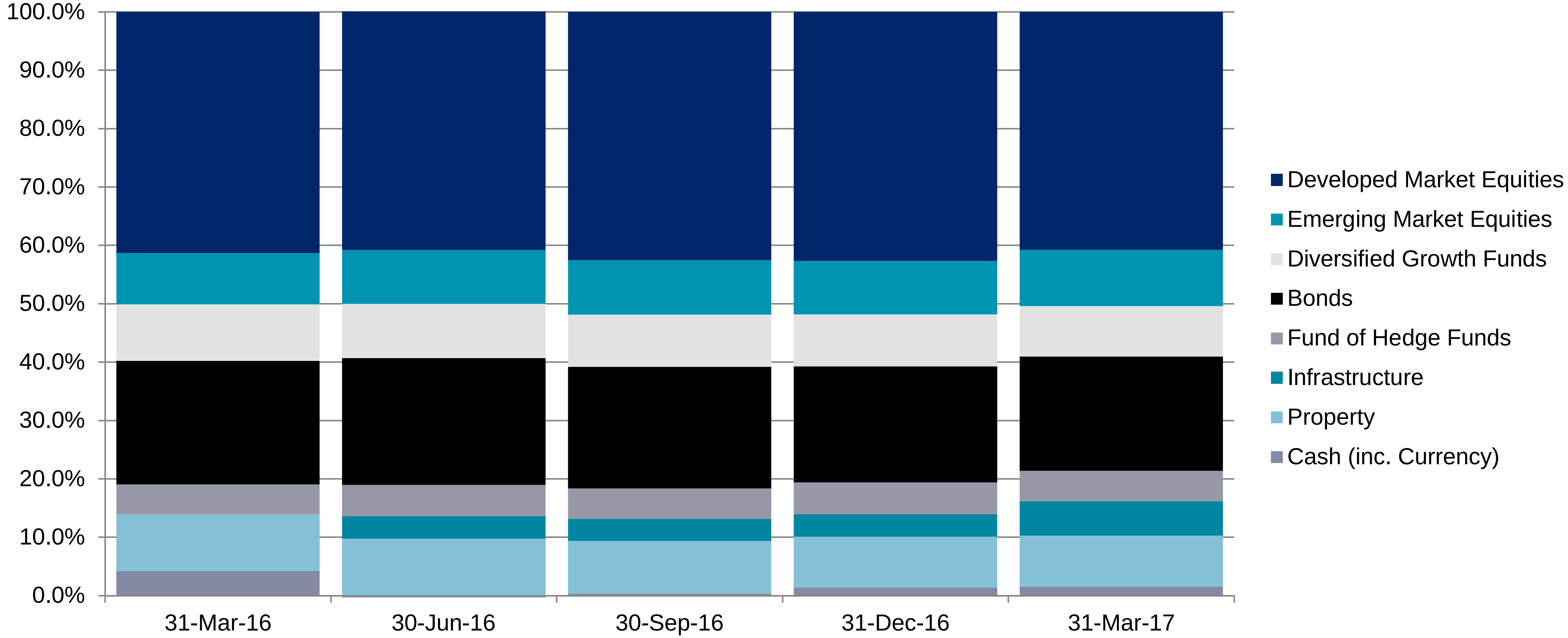
Source: BNY Mellon, Avon. Totals may not sum due to rounding.

FUND VALUATIONS
VALUATION BY MANAGER

Manager Allocation					
Manager	**Asset Class**	**31/03/2016 (£'000)**	**31/03/2017 (£'000)**	**31/03/2016 (%)**	**31/03/2017 (%)**
MAN	Fund of Hedge Funds	-	393	-	0.0
Signet	Fund of Hedge Funds	1,056	1,162	0.0	0.0
Gottex	Fund of Hedge Funds	3,547	971	0.1	0.0
JP Morgan	Fund of Hedge Funds	187,791	226,123	5.0	5.2
Schroder	UK Property	200,951	201,636	5.4	4.6
Partners	Property	161,950	192,361	4.3	4.4
IFM	Infrastructure	-	256,003	-	5.9
RLAM	Bonds	289,662	260,812	7.7	6.0
Record Currency Management	Currency Hedging	-29,277	10,323	-0.8	0.2
Internal Cash	Cash	169,023*	28,112	4.5	0.6
Total		**3,738,216**	**4,356,309**	**100.0**	**100.0**

Source: BNY Mellon, Avon. Totals may not sum due to rounding.
* Includes £136m transferred into the IFM infrastructure fund on 1 April 2016.

COMMENTARY ON CHANGE IN ASSET ALLOCATION OVER THE YEAR



There was one change to the Fund's asset allocation over the year. A new IFM Infrastructure fund, whose proceeds (£136m) were sourced from BlackRock developed market equities end March 2016, was funded on 1 June 2016. This was held as cash as at 31 March 2016. A further £84m was disinvested from BlackRock developed market equities and subsequently drawn down by IFM on 15 February 2017.

SECTION 4

MARKET BACKGROUND

MARKET BACKGROUND
INDEX PERFORMANCE OVER THE YEAR TO 31 MARCH 2017

Equity Market Review

Equities posted strongly positive returns as the ultra-accommodative monetary policy measures adopted by the world's major central banks continued to support financial markets. The strong returns posted by equities came despite bouts of volatility following the surprise result of the UK's referendum in June 2016, where the electorate voted to leave the European Union and the unexpected victory for Donald Trump in the US Presidential Election in November 2016. Over the 12 months to 31 March 2017, global equities as measured by the FTSE All World returned 33.1% in sterling terms and 17.9% in local currency terms (as sterling depreciated).

At a regional level, the major equity markets recorded strong returns in sterling terms. European markets returned 27.9%. UK stocks returned 22.0% while the FTSE Japan index returned 32.8%. The US and emerging markets equities were top performers, returning 35.2% and 35.6% respectively.

Bond Market Review

UK Government Bonds as measured by the FTSE Gilts All Stocks Index, returned 6.6%, while long dated issues as measured by the corresponding Over 15 Year Index had a return of 12.3% over the year. The yield for the FTSE Gilts All Stocks index fell over the year from 1.9% to 1.4%.

The FTSE All Stocks Index Linked Gilts index returned 19.9% with the corresponding over 15 year index exhibiting a return of 26.1%.

In a broad risk-on environment, credit spreads tightened over the year resulting in a total return of 9.3% for UK corporate bonds.

Currency Market Review

Over the 12 month period to 31 March 2017, Sterling fell by 13.0% against the US Dollar from $1.437 to $1.250. Sterling depreciated 13.75% against the Yen from ¥161.545 to ¥139.338. Sterling depreciated against the Euro by 7.3% from €1.261 to €1.164 over the same period.

Commodity Market Review

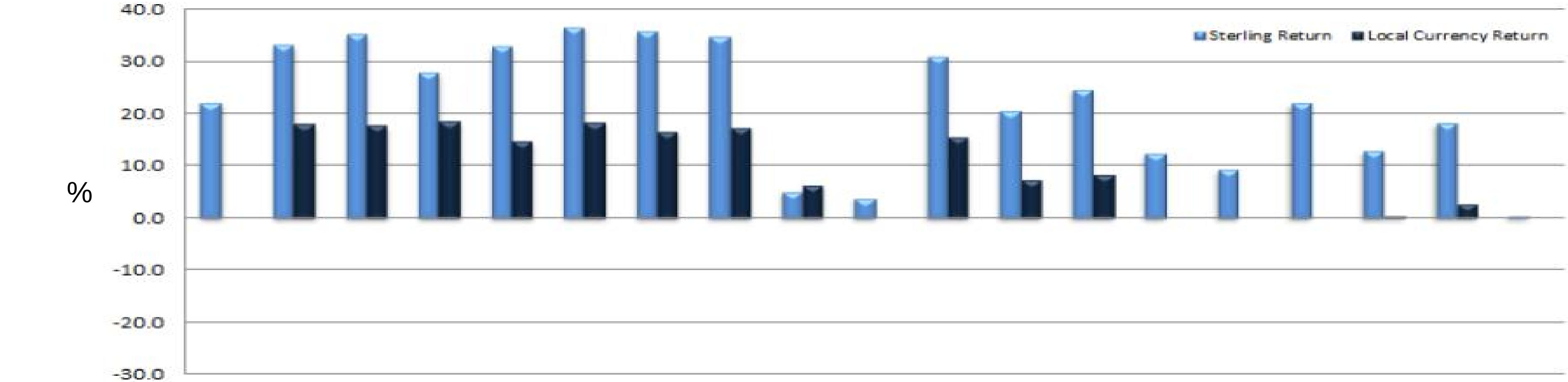
The price of Brent Crude increased by 31.7% from $39.95 to $52.62 per barrel over the one year period. Over the same period, the price of Gold rose 1.0% from $1234.34 per troy ounce to $1247.25.

The S&P GSCI Commodity Spot Index increased by 38.0% over the one year period to 31 March 2017 in Sterling terms.

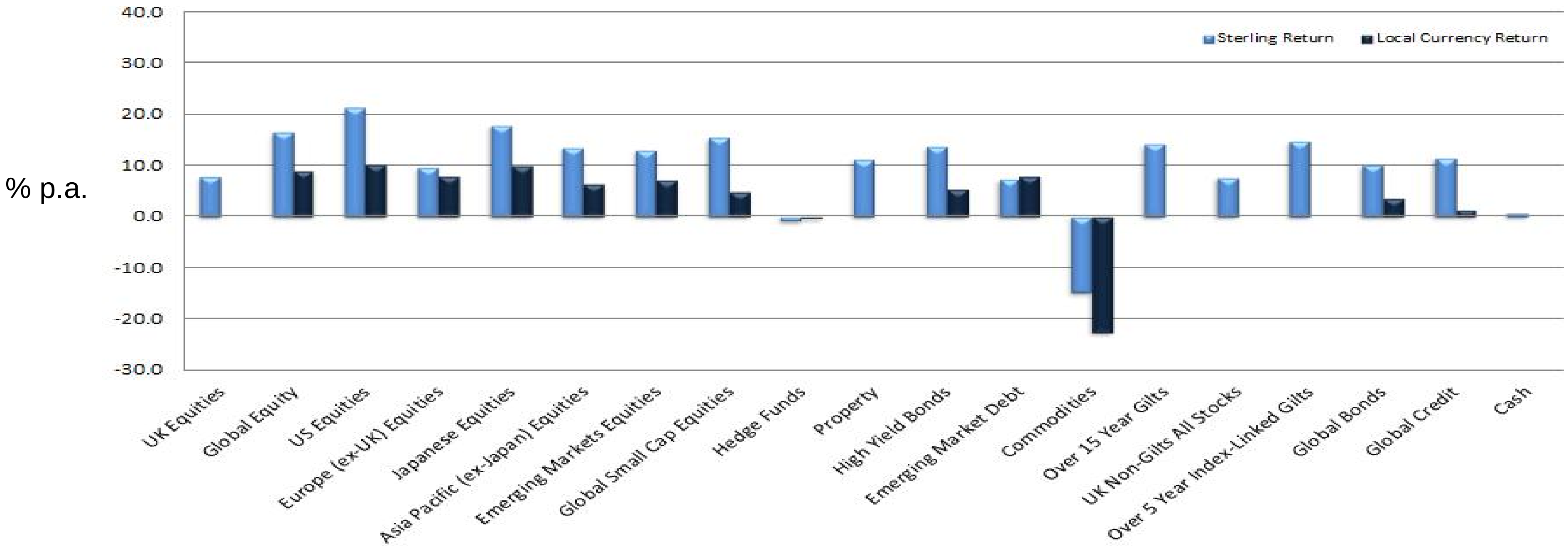
Source: Thomson Reuters Datastream.

MARKET BACKGROUND
INDEX PERFORMANCE

Return over the 12 months to 31 March 2017



Return p.a. over the 3 years to 31 March 2017

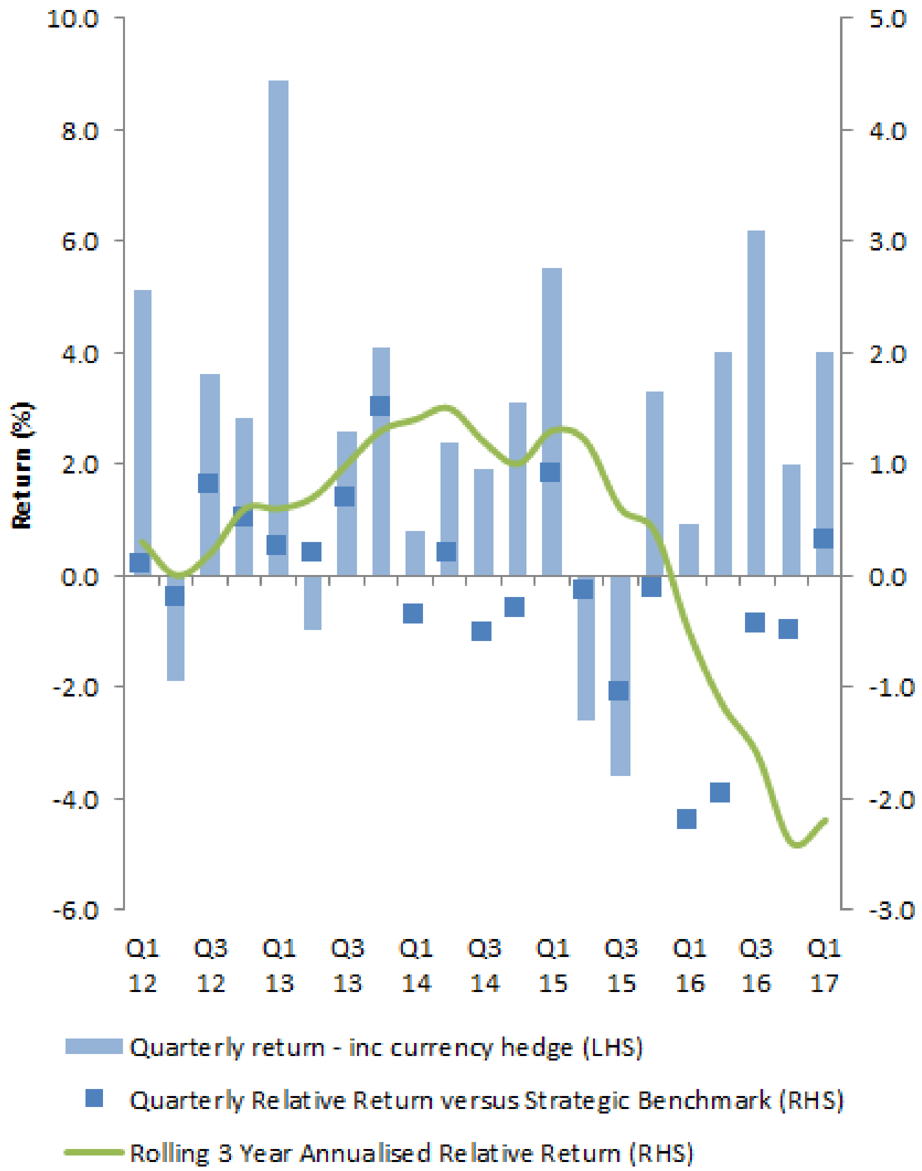


Source: Thomson Reuters Datastream.

SECTION 5

PERFORMANCE SUMMARY

PERFORMANCE SUMMARY
TOTAL FUND PERFORMANCE



	3 months (%)	1 year (%)	3 years (% p.a.)
Total Fund (inc currency hedge)	4.0	17.2	9.1
Total Fund (ex currency hedge)	3.8	20.2	10.8
Strategic Benchmark (no currency hedge)	3.7	20.1	11.3
Relative (inc currency hedge)	**+0.3**	**-2.9**	**-2.2**

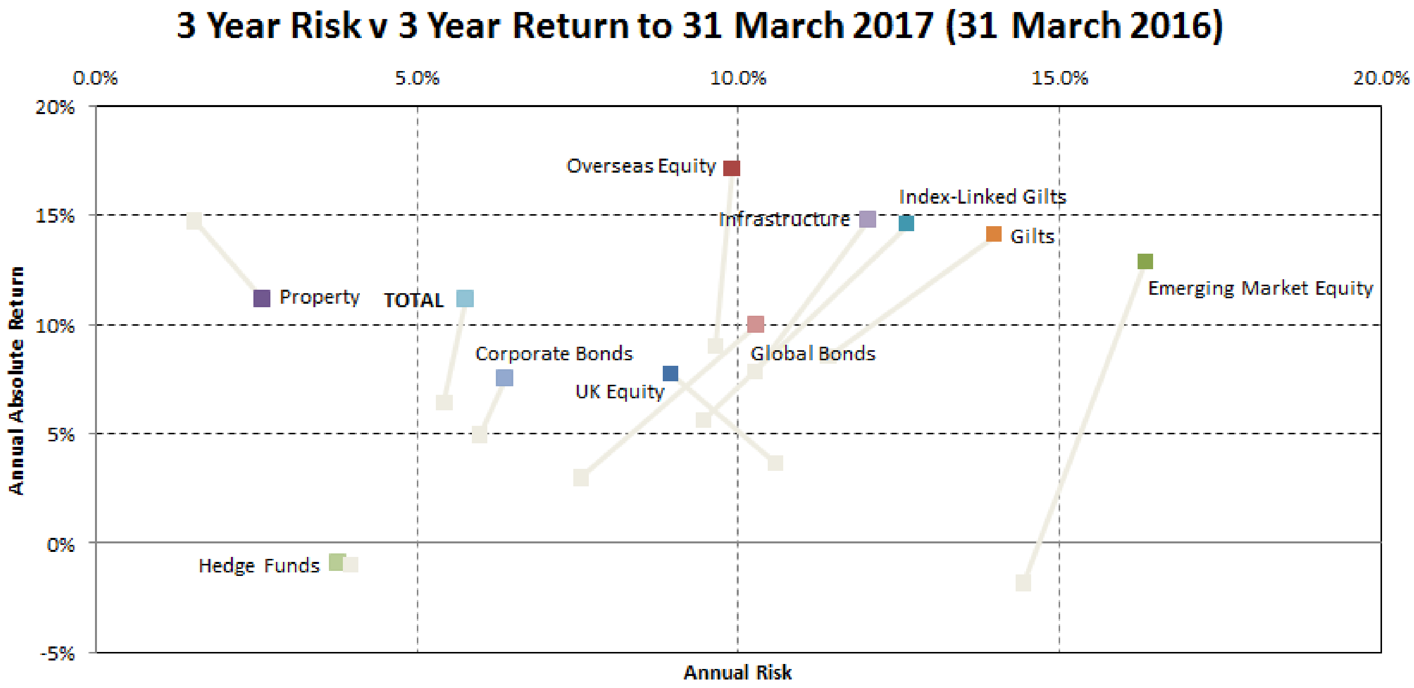
- Over the quarter, the Fund outperformed its Strategic Benchmark by 0.3% when including the currency hedge and by 0.1% excluding the currency hedge.
- Due to the underperformance over the last year, the rolling three year underperformance of the Fund increased to 2.2% p.a.
- The Fund marginally outperformed the unhedged strategic benchmark return (which excludes currency hedging) over the year. BlackRock and IFM were the main contributors to this performance whilst Unigestion, Standard Life and Jupiter were the main detractors.
- When the currency hedge with Record is included, the Fund underperformed due to the significant depreciation of sterling over the year.

PERFORMANCE SUMMARY
INDEX PERFORMANCE VS. STRATEGIC BENCHMARK

Asset Class	Weight in Strategic Benchmark (From April 2016)	Index returns	Contribution to total benchmark	Index returns	Contribution to total benchmark	Assumed strategic return	
	(%)	1 year (%)	1 year (%)	3 years (% p.a.)	3 years (% p.a.)	Return (% p.a.)	Contribution[1] (% p.a.)
UK Equities	**15.0**	22.0	3.3	**7.7**	1.2	**8.25**	0.0
Overseas Equities	**25.0**	33.4	8.3	**17.6**	4.6	**8.25**	2.5
Emerging Market Equities	**10.0**	35.2	3.5	**11.8**	1.3	**8.75**	0.4
Diversified Growth Funds	**10.0**	4.5	0.5	**4.5**	0.3	**4.6**	-0.1
UK Government Bonds	**0.0**	12.3	0.4	**14.0**	0.3	**4.5**	0.2
UK Corporate Bonds	**8.0**	9.3	0.7	**7.5**	0.6	**5.5**	0.2
Index Linked Gilts	**12.0**	22.0	1.3	**14.6**	1.3	**4.25**	1.0
Overseas Fixed Interest	**0.0**	11.3	0.3	**9.5**	0.2	**5.5**	0.1
Fund of Hedge Funds	**5.0**	4.5	0.2	**4.5**	0.2	**6.0**	-0.3
Property	**10.0**	3.7	0.4	**10.2**	1.1	**7.0**	0.4
Infrastructure	**5.0**	28.4	1.4	**14.8**	0.5	**7.0**	0.4
Total Fund	**100.0**		**20.1**		**11.3**	**6.9**	**4.4**

Source: BNY Mellon and Mercer estimates. May not sum due to rounding.
[1] Contribution to total difference between strategic benchmark return over last three years (11.3% p.a.) and overall assumed strategic return (6.9% p.a.) – weighted by strategic benchmark.

MANAGER MONITORING
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 2017, 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 BNY Mellon). We also show the positions as at 31 March 2016, in grey.

Comments

- The most significant shift in observed returns over the year was in emerging markets equities, whose 3 year return was negative a year ago.
- Index-linked gilts, gilts, global bonds and infrastructure also saw their returns rise but with a similar increased in volatility.
- Property was the only asset class whose return fell over the year.

ACTIVE INVESTMENT MANAGER CONTRIBUTION YEAR TO 31 MARCH 2017

Asset Cass	Weight in Strategic Benchmark Start (%)	Weight in Strategic Benchmark End (%)	Average Relative Position (%)	Fund Return (%)	Index Return (%)	Currency Impact * (%)	Asset Allocation Impact (%)	Active Manager Impact (%)	Total Manager Impact (%)
UK Equities	15.0	15.0	-1.6	18.0	22.0	+0.1	-0.2	-0.6	-0.6
Overseas Equities	25.0	25.0	2.5	33.4	32.6	+0.2	+0.1	+0.2	+0.5
Emerging Market Equities	10.0	10.0	-0.1	28.7	35.2	-	-0.1	-0.6	-0.7
Diversified Growth Funds	10.0	10.0	-0.8	3.8	4.5	-0.1	+0.2	-0.1	+0.1
UK Corporate Bonds	8.0	8.0	0.6	11.7	9.2	-0.1	+0.1	+0.2	+0.2
Index Linked Gilts	12.0	12.0	0.0	18.3	22.0	-	-0.1	-0.5	-0.6
Fund of Hedge Funds	10.0	5.0	-2.2	20.6	2.0	-	-0.1	+1.0	+1.0
Property	10.0	10.0	-0.8	9.0	12.7	+0.1	-	-0.4	-0.3
Infrastructure	0.0	5.0	1.5	22.4	3.0	-0.1	+0.3	+0.8	+1.0
Cash	0.0	0.0	1.1	-	-	-0.1	-3.4**	-	-3.5
Total Fund	**100.0**	**100.0**		**17.2**	**20.1**	**-**	**-3.1**	**+0.3**	**-2.9**

Source: BNY Mellon and Mercer estimates. May not sum due to rounding.
Average overweight position taken as the average of the beginning and end of year weights.
* This represents the impact currency volatility had at individual manager level, rather than at the total Fund return level.
** -3.0% of -3.4% cash asset allocation impact is attributable to the Funds currency hedge.

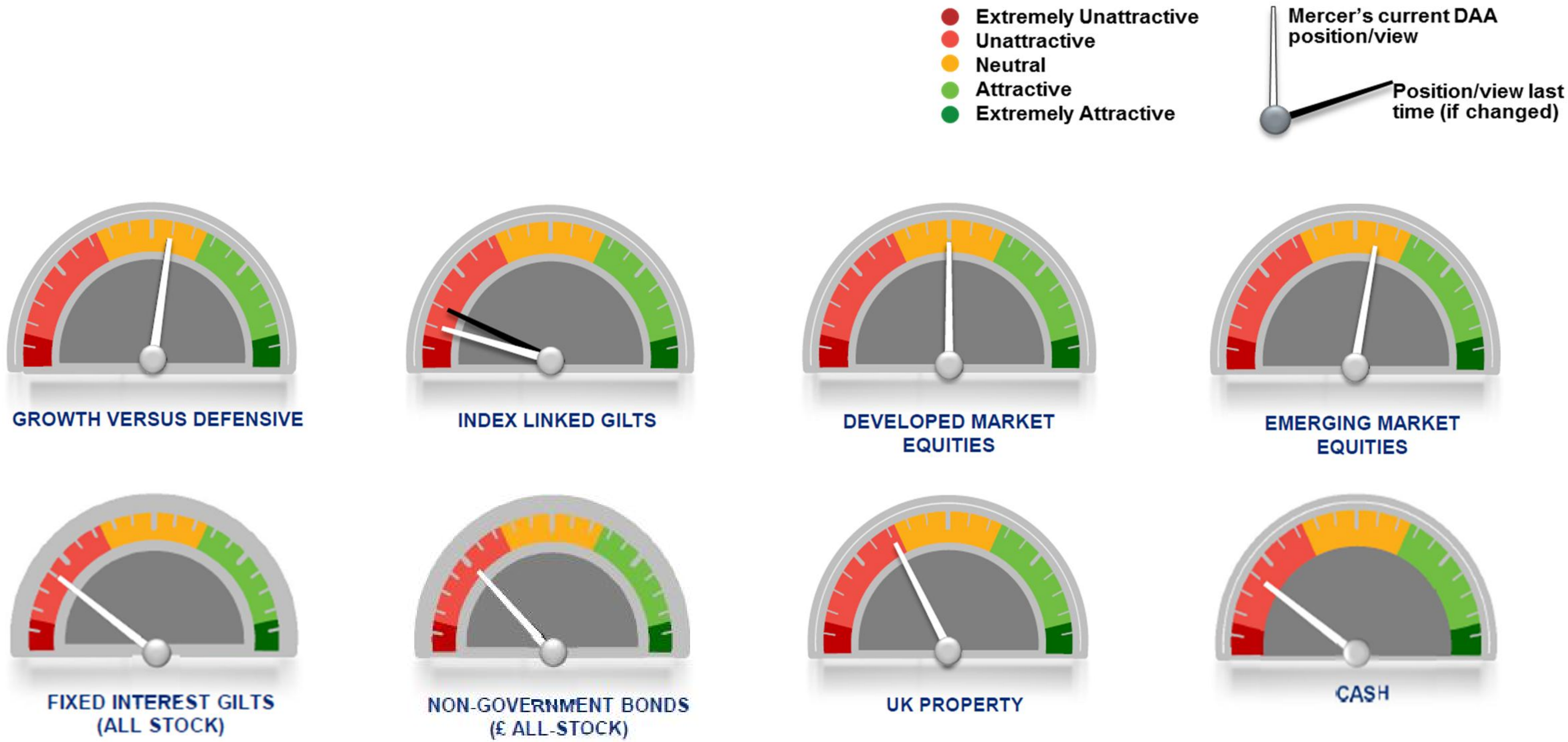
MANAGER MONITORING
MANAGER PERFORMANCE TO 31 MARCH 2017

Manager / fund	1 year (%)			3 year (% p.a.)			3 year outperformance target (% p.a.)	3 year performance versus target
	Fund	B'mark	Relative	Fund	B'mark	Relative		
BlackRock Multi-Asset	23.4	23.0	+0.4	13.0	12.7	+0.2	-	Target met
Jupiter	14.9	22.0	-5.8	7.5	7.7	-0.2	+2	Target not met
TT International	16.9	22.0	-4.1	8.3	7.7	+0.5	+3-4	Target not met
Schroder Equity	32.2	33.0	-0.6	15.7	16.3	-0.5	+4	Target not met
Genesis	31.7	35.2	-2.6	10.8	11.8	-0.9	-	Target not met
Unigestion	25.3	34.7	-7.0	10.2	11.4	-1.0	+2-4	Target not met
Invesco	34.0	32.6	+1.1	17.4	16.9	+0.4	+0.5	Target not met
SSgA Europe	29.9	28.0	+1.5	10.3	9.6	+0.6	+0.5	Target met
SSgA Pacific	35.7	34.7	+0.7	16.4	15.6	+0.7	+0.5	Target met
Pyrford	9.1	8.1	+0.9	6.0	6.9	-0.8	-	Target not met
Standard Life	0.6	5.6	-4.7	N/A	N/A	N/A	-	N/A
JP Morgan*	4.8	3.5	+1.2	N/A	N/A	N/A	-	N/A
Schroder Property	2.6	3.7	-1.1	10.0	10.2	-0.2	+1	Target not met
Partners Property	N/A	N/A	N/A	7.8**	10.0**	-2.0**	-	Target not met
IFM	N/A	N/A	N/A	6.7***	2.1***	+4.5***	-	N/A
RLAM	10.8	9.2	+1.5	8.0	7.5	+0.5	+0.8	Target not met
Internal Cash	-1.4	0.2	-1.6	-0.2	0.3	-0.5	-	N/A

- Source: BNY Mellon, Avon, Mercer estimates.
- Returns are in GBP terms, consistent with overall fund return calculations before currency hedging in applied, except for JP Morgan, Partners and IFM, whose performance is shown as IRR in local currency terms.
- In the relative performance columns, returns in blue text exceeded their respective benchmarks, those in red underperformed, and black text shows performance in line with benchmark.
- In the table above, and throughout this report, relative returns have been calculated geometrically (i.e. the portfolio return is divided by the benchmark return) rather than arithmetically (where the benchmark return is subtracted from the portfolio return).
- In the table above, Partners performance is measured against an IRR target of 10% p.a.
- A summary of the benchmarks for each of the mandates is given in Appendix 1.

* Performance is in US dollar terms.
** Performance is shown since inception and in local currency terms.
*** Performance is shown since inception and in US dollar terms.

FORWARD LOOKING RETURN EXPECTATIONS
31 MARCH 2017



The charts above summarise Mercer's views on the medium term (1-3 years) outlook for returns from the key asset classes. These views are relevant for reflecting medium term market views in determining appropriate asset allocation. We do not expect the Fund to make frequent tactical changes to their asset allocation based upon these views.

FORWARD LOOKING RETURN EXPECTATIONS CHANGES OVER THE LAST YEAR

Asset Class	Apr 2016	Jul 2016	Oct 2016	Jan 2017	Apr 2017
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	Neutral	Neutral	Neutral	Neutral	Neutral
Emerging Market Equities	Neutral	Neutral	Neutral	Neutral	Neutral
Small Cap Equities	Neutral	Neutral	Neutral	Neutral	Neutral
Low Volatility Equities	Neutral	Neutral	Neutral	Unattractive	Unattractive
UK Property	Neutral	Unattractive	Unattractive	Unattractive	Unattractive
High Yield Bonds	Neutral	Neutral	Unattractive	Unattractive	Unattractive
Local Currency Emerging Market Debt	Unattractive	Neutral	Neutral	Neutral	Neutral

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	14.9	22.0	-5.8	-0.30	7.5	7.7	-0.2	+2	-0.03
TT International	16.9	22.0	-4.1	-0.23	8.3	7.7	+0.5	+3-4	+0.02

Source: BNY Mellon / 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 22.0%, despite bouts of volatility following the surprise result of the UK's EU referendum in June 2016. This lagged global markets which returned 33.1% in sterling terms.

Performance Commentary

- Jupiter have underperformed the benchmark and target over the one and three year periods. Tracking error has stayed at 4.5% over the year. The fund underperformed the median UK active manager in Mercer's universe over the year.
- Jupiter's 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 significantly underperformed over the year by 4.1%, with sector allocation being a significant detractor from returns. The mandate outperformed over the three year period by 0.5% p.a., lagging the target.
- Over the year, the portfolio has held an underweight position in Financials, and security selection in that sector also proved to be poor.

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	34.0	32.6	+1.1	+0.09	17.4	16.9	+0.4	+0.5	+0.04
SSgA Europe	29.9	28.0	+1.5	+0.03	10.3	9.6	+0.6	+0.5	+0.01
SSgA Pacific	35.7	34.7	+0.7	+0.03	16.4	15.6	+0.7	+0.5	+0.02
Schroder	32.2	33.0	-0.6	-0.04	15.7	16.3	-0.5	+4	-0.04

Source: BNY Mellon / Mercer estimates.

Market Commentary

- Global equities returned 33.1% over the year in sterling terms, with strong performance across all the major regions: US equities delivered a return 35.2%, Europe 27.9%, Japan 32.8% and Asia Pacific 36.5% (all in sterling terms).

Performance Commentary

- Invesco outperformed over the year and three year periods by 1.1% and 0.4% p.a. vs an outperformance target of 0.5% p.a. Invesco's tracking error remains small at 1.2% 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 +/- 1.0% at 31 March 2017, with the exception of Financials, which were 1.1% underweight.
- Both SSgA funds outperformed over the year and three year periods.
- Schroder underperformed over the year and three year periods, with a three year tracking error of 2.5%.

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	31.7	35.2	-2.6	-0.13	10.8	11.8	-0.9	-	-0.05
Unigestion	25.3	34.7	-7.0	-0.38	10.2	11.4	-1.0	+2-4	-0.07

Source: BNY Mellon / Mercer estimates.

Market Commentary

- Emerging market equities, measured by FTSE All World Emerging, rose by 35.6% over the year, outperforming their developed market counterparts (FTSE All World Developed) which returned 32.9%, as headwinds from key economies (e.g. China) diminished, fundamentals and resilience to developed market shocks improved and export growth accelerated.

Performance Commentary

- Genesis underperformed by 2.6% over the year. This is not unexpected due to their style. This was largely due to underperformance in Q3 2016 and Q1 2017, when the portfolio's Indian and Russian holdings detracted respectively. The fund also underperformed over the three years, by 0.9% p.a.
- Unigestion underperformed by 7.0% over the year, having lagged its benchmark over every quarter. This is not unexpected due to their style. Over the three years the fund underperformed by 1.0% p.a., with lower volatility than the benchmark (14.9% p.a. vs 17.9% p.a.). The largest regional weighting of the portfolio is in South Korea (c. 22%) and the vast majority of holdings (c. 82%) are in mega- or large-cap stocks.

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
JP Morgan	4.8	3.5	+1.2	+0.07	N/A	N/A	N/A	-	N/A

Source: BNY Mellon / JP Morgan / Mercer estimates. Returns are in US dollar terms.

Market Commentary [1]

- Fund of Hedge Funds have generally lagged equity markets over the year and three years; over the year to 31 March 2017 the HFRI index rose 5.2%, the HFRX index returned 6.2% and the Dow Jones Credit Suisse Hedge Fund Index returned 5.7%.
- Looking at specific sectors, relative value strategies produced positive returns with fixed income and convertible arbitrage strategies returning 8.0% and 9.4% over the year.
- Long/short equity strategies benefitted from positive market tailwinds returning 3.9%, while market neutral strategies detracted returned -2.2% over the year. Event driven strategies improved over the last 12 months, returning 10.4%, driven by a robust overall volume of deals.
- The broad global macro universe also produced positive returns (of 6.2%) in low volatile markets.
- We continued to see dispersion in manager results across strategies.

Performance Commentary

- JP Morgan returned 4.8% over the year (in US dollar terms), against a benchmark of 3.5%. Long/short equity and credit strategies were the biggest contributors to performance over the period.

[1] Returns are in US dollar terms; source: Credit Suisse Hedge Index LLC.

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	23.4	23.0	+0.4	+0.14	13.0	12.7	+0.2	-	+0.02
Pyrford	9.1	8.1	+0.9	+0.03	6.0	6.9	-0.8	-	-0.02
Standard Life	0.6	5.6	-4.7	-0.31	N/A	N/A	N/A	-	N/A

Source: BNY Mellon / Mercer estimates.

Performance Commentary

- The passive multi-asset mandate managed by BlackRock continues to perform broadly in line with underlying indices (as expected).
- Over the last year, equity and bond markets produced positive returns. Pyrford outperformed its benchmark by 0.9% while Standard Life significantly underperformed by 4.7%.
- The benchmark used for the DGFs includes their outperformance target above cash. Growth asset returns over the year have been strong, meaning opportunities to hit the high performance targets have been wide. These targets are set over the longer term and conclusions cannot be drawn over a 12 month period.
- Pyrford has decreased its allocation to equities over the year (from 37% to 31%). This decision was made by Pyrford's Investment Strategy Committee in Q3 2016 reflecting its view that there is very little fundamental value in equities. The target allocation is now 30% in equities, 67% in fixed income and 3% in cash.
- It has been a difficult period for Standard Life since the Fund's investment was made - five out of eight quarters have seen negative absolute performance.

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	10.8	9.2	+1.5	+0.09	8.0	7.5	+0.5	+0.8	+0.04

Source: BNY Mellon / Mercer estimates.

Market Commentary

- In a broad risk-on environment, credit spreads tightened over the year resulting in a total return of 9.3% for UK corporate bonds. Gilt yields decreased over the period.

Performance Commentary

- RLAM have outperformed the benchmark over the year by 1.5% and over the three year period by 0.5%, meaning they failed to meet the performance target.
- Relative to the benchmark the portfolio has a shorter duration (8.0 years vs 8.2), a higher weighted average gross redemption yield (2.8% vs 2.1%) and a significantly more concentrated portfolio of stocks (at 271 vs 1,013).
- 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 outperform investment grade credit).

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	2.6	3.7	-1.1	-0.04	10.0	10.2	-0.2	+1	0.00
Partners	N/A	N/A	N/A	N/A	7.8 *	10.0 *	-2.0 *	+2	N/A

Source: BNY Mellon / Partners / Mercer estimates.
* Performance is shown since inception and in local currency terms.

Market Commentary

- The UK property market returned 3.7% over the year (measured by the UK IPD PPF All Balanced Funds Index – the benchmark for the Schroder mandate). UK property investors continue to benefit from the improving property market.
- Partners' performance target is 10% p.a. and benchmark taken as 8% p.a. (estimated net IRR, in local currency terms).

Performance Commentary

- Schroder underperformed the benchmark over the year and three year periods.
- However, over the five year period, Schroder has outperformed its benchmark by 0.6% p.a. (9.1% against a benchmark of 8.5%), largely due to performance from Value Add strategies.
- 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 March 2017 at 7.8% p.a. (in local currency) is below their target of 10% p.a.

MANAGER MONITORING INFRASTRUCTURE

Manager / fund	1 Year (%)				3 years (% p.a.) *				
	Fund	B'mark	Relative	Contribution to outperformance	Fund	B'mark	Relative	Target	Contribution to outperformance
IFM	N/A	N/A	N/A	N/A	6.7	2.1	+4.5	-	+0.14

Source: BNY Mellon / IFM / Mercer estimates. Returns are in US dollar terms.
* Returns since inception on 1 June 2016 shown as fund has not been invested for the whole period.

Market Commentary

- The infrastructure market was strong over the year, returning 28.4% as measured by the S&P Global Infrastructure Index in sterling terms. Returns of this index have been largely driven by currency moves. The 100% hedge in place for the infrastructure mandate removes the currency effect from the actual returns earned.

Performance Commentary

- Over the period since inception to 31 March 2017, IFM outperformed its benchmark (cash + 2.5% p.a.) in US dollar terms.
- All the capital committed has been drawn down by IFM until Q1 2017.
- The portfolio consists of 13 holdings and nearly half of it is invested in the United States. Toll roads and airports represent the main sub-sector allocations of the fund.

MANAGER MONITORING CURRENCY

Market Commentary

- Over the 12 month period to 31 March 2017, Sterling fell by 13.0% against the US Dollar from $1.437 to $1.250. Sterling depreciated 13.75% against the Yen from ¥161.545 to ¥139.338. Sterling depreciated against the Euro by 7.3% from €1.261 to €1.164 over the same period.
- Sterling depreciated sharply against its major counterparts following the 'Brexit' vote. This led to material gains for unhedged Sterling investors in foreign assets.

Performance Commentary

- Following the investment in the IFM Infrastructure fund, a new passive mandate was initiated to hedge 100% of the currency exposure on infrastructure.
- Over the 12 month period to 31 March 2017, the hedging mandates have all slightly outperformed their informal benchmark returns.

Currency Hedging 12 Month Performance (£ terms)

Passive Developed Equity Hedge

Currency	Start Exposure (£)	End Exposure (£)	Currency Return (%)	50% Benchmark Return (%)	Record Hedge Return (%)	Net Return (%)
USD	572,761,642	566,546,627	14.94%	(7.53%)	(7.40%)	7.26%
EUR	188,644,012	186,052,434	7.88%	(3.80%)	(3.76%)	4.57%
JPY	130,089,526	135,640,419	15.94%	(8.32%)	(8.17%)	8.75%
Total	**891,495,180**	**888,239,480**	**13.66%**	**(6.83%)**	**(6.71%)**	**6.91%**

Passive Hedge Fund Hedge

Currency	Start Exposure (£)	End Exposure (£)	Currency Return (%)	100% Benchmark Return (%)	Record Hedge Return (%)	Net Return (%)
USD	194,312,572	226,422,372	14.94%	(15.18%)	(14.98%)	(0.45%)
Total	**194,312,572**	**226,422,372**	**14.94%**	**(15.18%)**	**(14.98%)**	**(0.45%)**

Passive Property Hedge

Currency	Start Exposure (£)	End Exposure (£)	Currency Return (%)	100% Benchmark Return (%)	Record Hedge Return (%)	Net Return (%)
USD	36,421,737	36,735,954	14.94%	(15.25%)	(14.97%)	(0.43%)
EUR	134,164,968	147,562,492	7.88%	(7.94%)	(7.87%)	0.69%
Total	**170,586,705**	**184,298,446**	**9.33%**	**(9.44%)**	**(9.32%)**	**0.46%**

Passive Infrastructure Hedge *- started on 17 May 2016*

Currency	Start Exposure (£)	End Exposure (£)	Currency Return (%)	100% Benchmark Return (%)	Record Hedge Return (%)	Net Return (%)
USD	69,295,032	145,827,716	15.53%	(15.56%)	(15.40%)	(0.56%)
EUR	15,114,049	28,275,512	8.96%	(8.94%)	(9.01%)	0.35%
Total	**84,409,081**	**174,103,228**	**14.52%**	**(14.54%)**	**(14.42%)**	**(0.42%)**

APPENDIX 2
SUMMARY OF MANDATES

SUMMARY OF MANDATES

Manager	Mandate	Benchmark	Outperformance target (p.a.)
BlackRock	Passive Multi-Asset	In line with customised benchmarks using monthly mean fund weights	-
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%
Pyrford	Diversified Growth Fund	RPI +5% p.a.	-
Standard Life	Diversified Growth Fund	6 Month LIBOR +5% p.a.	-
JP Morgan	Fund of Hedge Funds	3 Month LIBOR +3% p.a.	-
Schroder	UK Property	IPD UK Pooled	+1%
Partners	Overseas Property	Net IRR of 10% p.a. (local currency)	-
IFM	Infrastructure	6 Month LIBOR +2.5% p.a.	-
Royal London Asset Management	UK Corporate Bonds	iBoxx £ Non-Gilts All Maturities	+0.8%
Record	Passive Currency Hedging	N/A	-
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
Infrastructure	S&P Global Infrastructure
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.

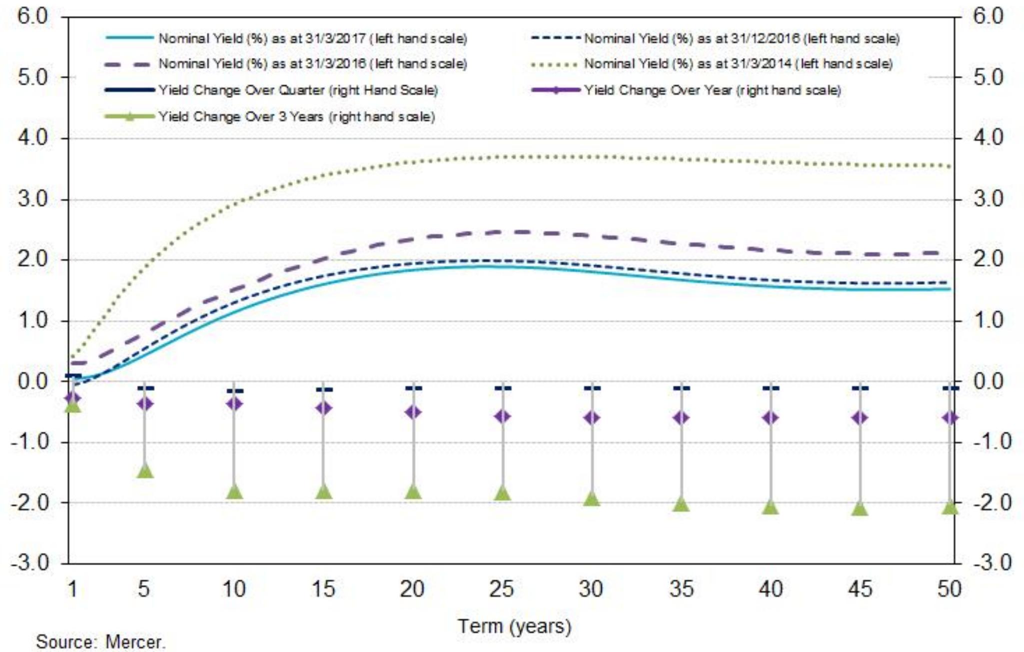
APPENDIX 4
CHANGES IN YIELDS

CHANGES IN YIELDS

Asset Class Yields (% p.a.)	31 Mar 2017	31 Dec 2016	31 Mar 2016	31 Mar 2015
UK Equities	3.47	3.47	3.77	3.33
Over 15 Year Gilts	1.65	1.76	2.17	2.23
Over 5 Year Index-Linked Gilts	-1.71	-1.66	-0.97	-0.91
Sterling Non Gilts	2.20	2.29	2.90	2.65

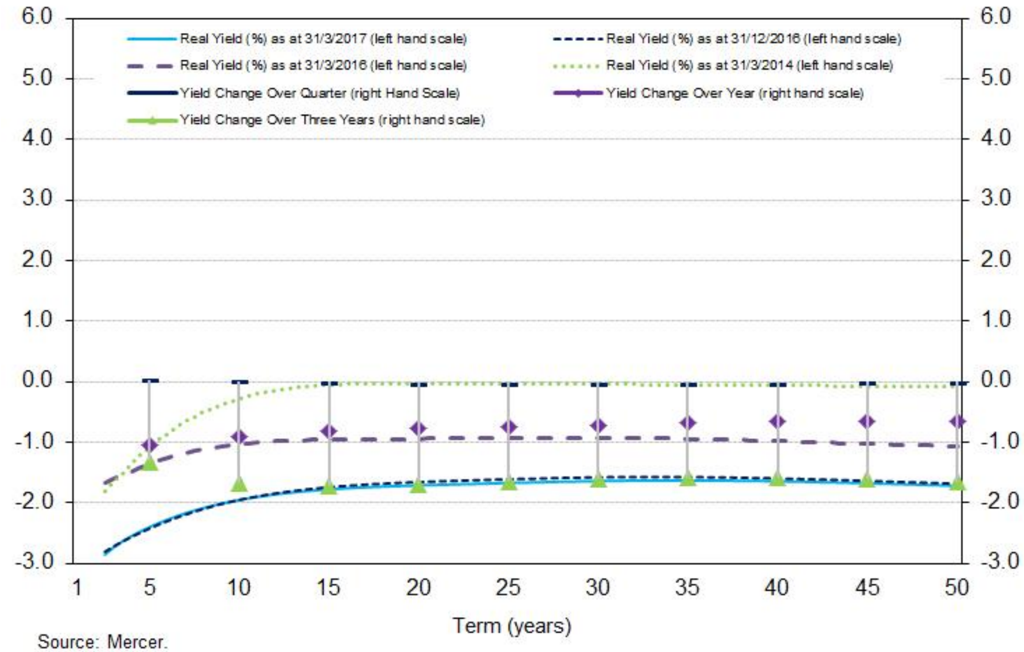
- UK Government Bonds as measured by the FTSE Gilts All Stocks Index, returned 6.6%, while long dated issues as measured by the corresponding Over 15 Year Index had a return of 12.3% over the year. The yield for the FTSE Gilts All Stocks index fell over the year from 1.9% to 1.4%.
- The FTSE All Stocks Index Linked Gilts index returned 19.9% with the corresponding over 15 year index exhibiting a return of 26.1%.
- In a broad risk-on environment, credit spreads tightened over the year resulting in a total return of 9.3% for UK corporate bonds.

Nominal yield curves



Source: Mercer.

Real yield curves



Source: Mercer.

APPENDIX 5
HEDGE FUND INDICES

HEDGE FUND INDICES

HFRI Diversified Fund of Fund Index

- The Diversified Fund of Fund Index is an equally-weighted index comprising fund of fund managers that satisfy the following criteria: Invest in a variety of strategies across multiple managers, exhibit standard deviation and returns correlation similar to the HFR Fund of Funds composite index.
- The trailing four months' performance figures are left as estimates and are subject to change; performance beyond four months is locked and not subject to change.
- If a fund liquidates or closes, that fund's performance will be included in the index as of the fund's last reported performance.
- There is no minimum asset size or minimum track record length requirement for inclusion in the index.
- Both domestic and offshore funds are included.

HFRX Global Hedge Fund Index

- The HFRX Global Hedge Fund Index is an "investible" index designed to be representative of the overall composition of the hedge fund universe (it is termed "investible" because investors are able to access all of the underlying funds and as such generate a return in line with the index).
- It is comprised of eight strategies: convertible arbitrage, merger arbitrage, equity hedge, equity market neutral, relative value arbitrage, event driven, distressed securities, and global macro.
- The strategies are asset weighted based on the distribution of assets in the hedge fund industry.

Credit Suisse Hedge Fund Index

- The Credit Suisse Hedge Fund Index (formerly the Dow Jones Credit Suisse/Tremont Hedge Fund Index) is an asset weighted index of hedge funds.
- Funds in the Dow Jones Credit Suisse Hedge Fund universe must have a minimum of US $10 million assets under management ("AUM"), a minimum one-year track record and current audited financial statements.

MERCER

MAKE
TOMORROW,
TODAY