

MERTON PENSION FUND
INVESTMENT PERFORMANCE REVIEW
QUARTER ENDING 31 DECEMBER 2018

1 STRATEGIC ASSET ALLOCATION

31 DECEMBER 2018

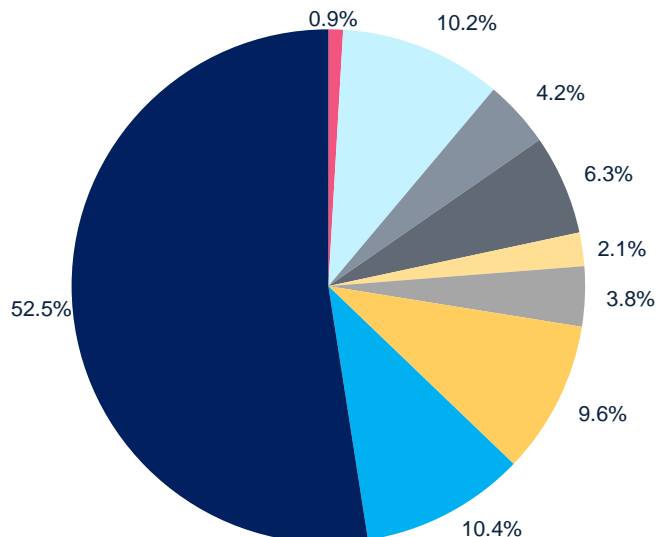
Allocation by underlying asset class

Asset Class	Market Value £000s	Actual Weight %	Strategic Allocation %	Relative %	Strategic Range %
Global Equities	347,378	52.5	40.0	12.5	15-85
Emerging Market Equities	68,606	10.4	10.0	0.4	0-20
Diversified Growth Fund	63,806	9.6	10.0	-0.4	0-20
Property	24,981	3.8	5.0	-1.2	0-10
Private Credit	-	0.0	7.5	-7.5	0-10
Infrastructure	-	0.0	7.5	-7.5	0-15
Long Gilts	14,009	2.1	-	2.1	0-5
Long Index Linked Gilts	41,600	6.3	10.0	-3.7	0-30
Corporate Bonds	28,051	4.2	-	4.2	0-10
Multi Asset Credit	67,572	10.2	10.0	0.2	0-20
Cash	6,078	0.9	-	0.9	-
TOTAL MERTON PENSION FUND	662,083	100.0	100.0	-	

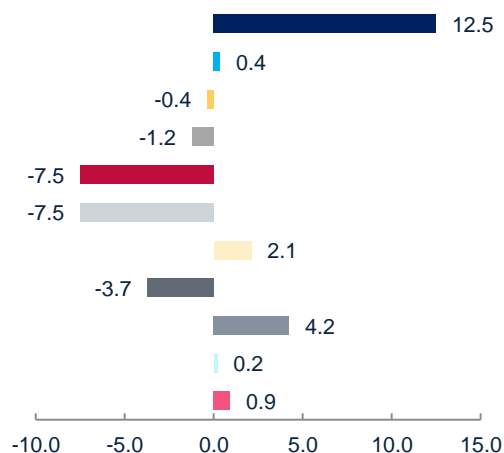
Points to note

- The Strategic Asset Allocation reflects the strategy to be implemented as part of the 2017 Investment Strategy Review; as such a number of asset classes will be under or overweight for an interim period until the portfolio is fully constructed.
- Total allocation to Global Equities decreased to 52.5% over the quarter, thereby is 12.5% overweight relative to its strategic allocation. However, this allocation will fall over time as the Fund transitions to Private Credit and Infrastructure.

Actual Asset Allocation as at 31 December 2018



Deviation from Strategic Allocation



2 VALUATION SUMMARY

30 SEPT 2018 TO 31 DEC 2018

Manager / Fund	30-September-18				31-December-18	
	Valuation £000s	Weight %	Cashflow £000s	Growth £000s	Valuation £000s	Weight %
UBS - Passive Equity	243,888	34.4	-134,609	-19,916	89,363	13.5
UBS – Alternative Beta	-	-	68,000	-3,357	64,643	9.8
UBS - Active Equity Fund	44,734	6.3	-41,391	-3,343	-	0.0
LCIV RBC Sustainable Equity Fund	74,879	10.6	-	-9,025	65,854	9.9
LCIV Global Alpha Growth Fund	72,244	10.2	-	-9,009	63,235	9.6
BlackRock World Low Carbon Equity Tracker Fund	-	-	68,000	-3,718	64,282	9.7
Global Equities	435,745	61.5			347,378	52.5
Aberdeen Emerging Market Equities Fund	27,777	3.9	-	-474	27,302	4.1
UBS – HALO EM Fund	-	-	40,000	1,304	41,304	6.2
Emerging Market Equities	27,777	3.9			68,606	10.4
LCIV Global Total Return Fund	33,461	4.7	-	-675	32,786	5.0
LCIV Diversified Growth Fund	32,493	4.6	-	-1,473	31,020	4.7
Diversified Growth Fund	65,954	9.3			63,806	9.6
UBS Triton Property Unit Trust	16,831	2.4	-	177	17,008	2.6
BlackRock UK Property Fund	7,875	1.1	-	98	7,973	1.2
Property	24,706	3.5			24,981	3.8
Growth Assets	554,182	78.2			504,772	76.2
Aberdeen Bonds	81,895	11.6	-	1,766	83,661	12.6
Bonds	81,895	11.6			83,661	12.6
LCIV MAC Fund	68,952	9.7	-	-1,380	67,572	10.2
Multi Asset Credit	68,952	9.7			67,572	10.2
Stabilising Assets	150,847	21.3			151,233	22.8
Cash	3,319	0.5	2,759	-	6,078	0.9
TOTAL MERTON PENSION FUND	708,349	100.0			662,083	100.0

NOTE: INCOME REINVESTED BY LCIV FUNDS IN THE QUARTER AMOUNTED TO £0.9M.

3 PERFORMANCE SUMMARY

PERIOD ENDING 31 DECEMBER 2018

Manager / Fund	3 months %		12 months %		3 years % p.a.		3yr Performance
	Fund	Bmark	Fund	Bmark	Fund	Bmark	vs. Bmark
UBS - Passive Equity Fund †	-11.4	n/a	-7.4	n/a	8.6	n/a	n/a
UBS – Alternative Beta*	-5.0	-4.9	n/a	n/a	n/a	n/a	n/a
LCIV RBC Sustainable Equity Fund	-12.0	-11.4	n/a	n/a	n/a	n/a	n/a
LCIV Global Alpha Growth Fund	-12.5	-10.6	n/a	n/a	n/a	n/a	n/a
BlackRock World Low Carbon Equity Tracker Fund*	-5.5	-5.5	n/a	n/a	n/a	n/a	n/a
Global Equities							
Aberdeen Global Emerging Market Equities Fund	-1.4	-5.2	n/a	n/a	n/a	n/a	n/a
UBS – HALO EM Fund*	3.1	2.2	n/a	n/a	n/a	n/a	n/a
Emerging Market Equities							
LCIV Global Total Return Fund	-2.0	1.8	n/a	n/a	n/a	n/a	n/a
LCIV Diversified Growth Fund	-4.6	1.1	n/a	n/a	n/a	n/a	n/a
DGF							
UBS Triton Property Unit Trust	1.6	0.9	8.7	6.5	7.2	6.4	Benchmark met
BlackRock UK Property Fund	1.2	0.9	6.6	6.5	6.4	6.4	Benchmark met
Property							
Growth Assets							
Aberdeen Bonds Portfolio	2.4	2.4	1.1	0.9	8.3	8.3	Benchmark met
Bonds							
LCIV MAC Fund	-2.0	1.2	n/a	n/a	n/a	n/a	n/a
Multi-Asset Credit							
Stabilising Assets							
TOTAL MERTON PENSION FUND							
	-6.5		-3.9		9.3		
Strategic Target (5.5% p.a.)	1.3		5.5		5.5		

* Partial quarter performance shown. These funds were entered into in mid-October 2018 and hence the fund and benchmark returns are not reflecting the entire of Q4 2018.

† Benchmark suspended in Q2 2018 as a result of transition activity. This impacts 3 month, 12 month and 3 year benchmark returns.

4 MARKET BACKGROUND

PERIOD ENDING 31 DECEMBER 2018

MARKET STATISTICS

Market Returns Growth Assets	3 Mths %	1 Year %	3 Years % p.a.
UK Equities	-10.2	-9.5	6.1
Overseas Developed	-11.0	-2.7	12.9
North America	-11.5	0.8	14.6
Europe (ex UK)	-11.0	-9.1	8.4
Japan	-12.4	-7.6	9.1
Asia Pacific (ex Japan)	-7.6	-8.7	12.9
Emerging Markets	-3.9	-7.6	14.8
Frontier Markets	-4.1	-15.3	5.9
Property	0.9	6.6	6.8
Hedge Funds**	-6.2	-6.2	1.8
Commodities**	-23.4	-15.5	-1.0
High Yield**	-3.9	-3.7	5.9
Emerging Market Debt	4.6	-0.4	11.2
Senior Secured Loans**	-4.9	-2.3	3.2
Cash	0.2	0.6	0.4

Yields as at 31 December 2018	% p.a.
UK Equities	4.46
UK Gilts (>15 yrs)	1.76
Real Yield (>5 yrs ILG)	-1.59
Corporate Bonds (>15 yrs AA)	2.77
Non-Gilts (>15 yrs)	3.36

Market Returns Bond Assets	3 Mths %	1 Year %	3 Years % p.a.
UK Gilts (>15 yrs)	2.6	0.3	7.1
Index-Linked Gilts (>5 yrs)	2.0	-0.4	9.2
Corporate Bonds (>15 yrs AA)	1.4	-1.9	7.0
Non-Gilts (>15 yrs)	-0.5	-4.1	6.4

Exchange Rates: Change in Sterling	3 Mths %	1 Year %	3 Years % p.a.
Against US Dollar	-2.3	-5.9	-4.8
Against Euro	-0.8	-1.1	-6.4
Against Yen	-5.7	-8.3	-7.6

Inflation Indices	3 Mths %	1 Year %	3 Years % p.a.
Price Inflation – RPI	0.5	2.7	3.1
Price Inflation – CPI	0.5	2.1	2.2
Earnings Inflation*	0.2	3.4	2.8

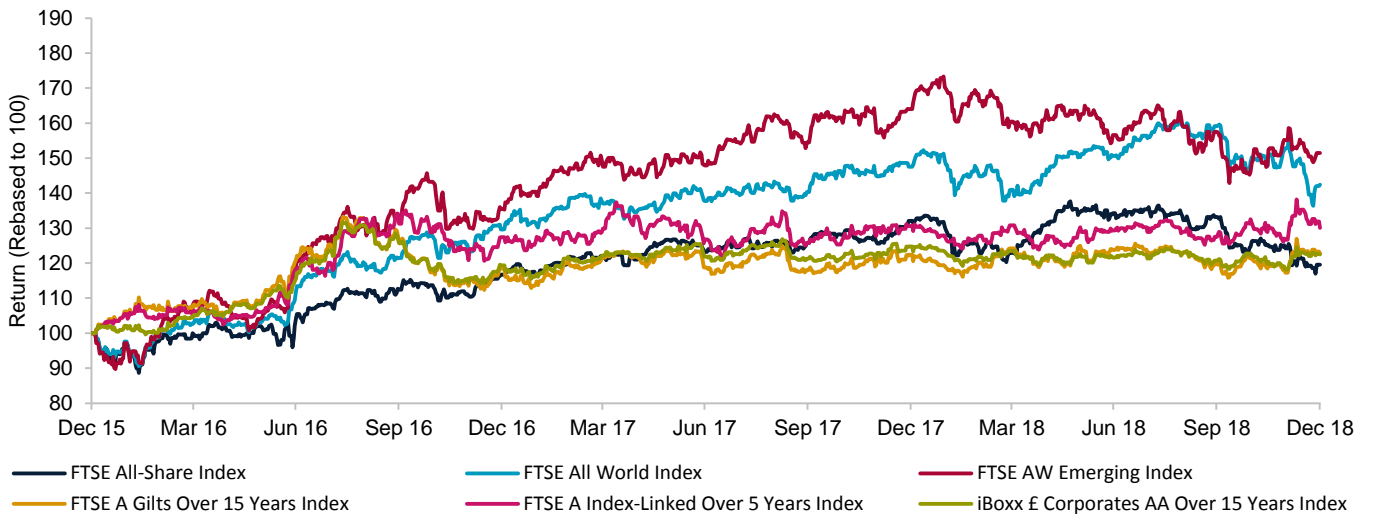
Absolute Change in Yields	3 Mths %	1 Year %	3 Years % p.a.
UK Equities	0.66	0.87	0.76
UK Gilts (>15 yrs)	-0.10	0.08	-0.81
Real Yield (>5 yrs ILG)	-0.09	0.08	-0.88
Corporate Bonds (>15 yrs AA)	-0.04	0.33	-0.92
Non-Gilts (>15 yrs)	0.09	0.46	-0.64

Source: Thomson Reuters.

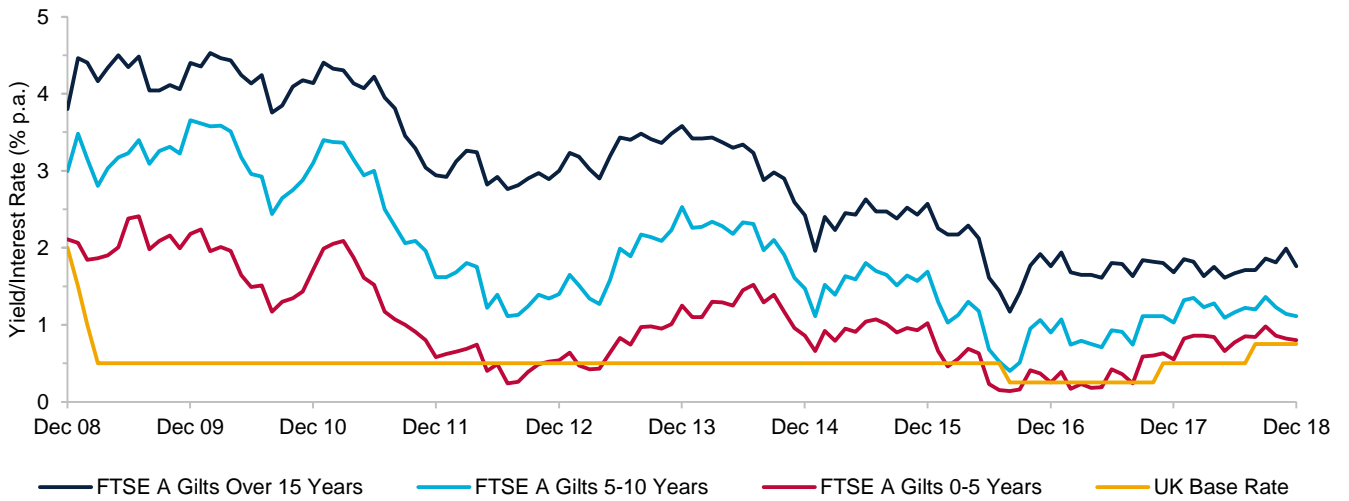
Note: * Subject to 1 month lag ** GBP Hedged

MARKET SUMMARY CHARTS

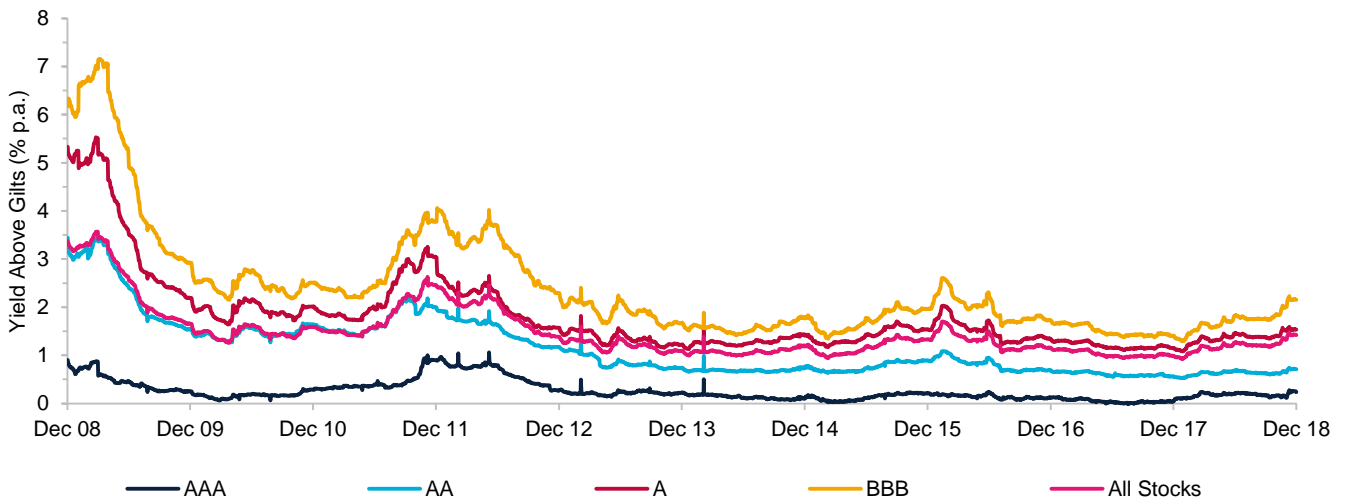
Market performance – 3 years to 30 September 2018



UK government bond yields – 10 years to 30 September 2018



Corporate bond spreads above government bonds – 10 years to 30 June 2018



Source: Thomson Reuters

5 MARKET EVENTS

Asset Class	What happened?	
	Positive Factors	Negative Factors
United Kingdom	<ul style="list-style-type: none"> The Purchasing Managers' Index (PMI) for the manufacturing sector grew at the fastest pace since June 2018. The IHS Markit UK Services PMI Index posted 51.2 in December, up from 50.4 in November. 	<ul style="list-style-type: none"> UK equities fell over the quarter on the back of concerns about a slowdown in the global economy and increased political and economic uncertainty regarding Brexit.
North America	<ul style="list-style-type: none"> The Bureau of Economic Analysis reported that the US GDP grew at a rate of 3.5% YoY in Q3, slightly lower than the growth posted in Q2. 	<ul style="list-style-type: none"> Persistent US-China trade conflicts and an expected slowdown in the global economy are likely to affect sales and earnings growth in 2019. The US Fed raised rates by another quarter point in December and signalled two more rate hikes in 2019.
Europe (ex UK)	<ul style="list-style-type: none"> Economic growth in the Eurozone continued to remain positive with the Q3 2018 GDP growing at 1.7% YoY. While the growth rate has moderated slightly, it remains healthy and is expected to remain so over the rest of the year. 	<ul style="list-style-type: none"> Inflation in the Eurozone slumped to an eight-month low in December. The annual headline inflation number came in at 1.6%, down from the high of 2.1% seen in September. Disappointingly core inflation still remains subdued at 1.0%, significantly below the ECB's target of 2.0%. The European Central Bank (ECB) has confirmed that it will be ceasing its quantitative easing programme from December 2019. It has also left the door open to rate hikes in 2019.
Japan	<ul style="list-style-type: none"> Low valuation and the ultra loose monetary policy of the Bank of Japan is providing some support to equity markets. Fundamentals such as RoE, RoA and debt levels are expected to largely remain stable in 2019. 	<ul style="list-style-type: none"> Lower than expected domestic and overseas demand owing to low wage growth, proposed tax hike and a slowing global economy. An appreciating Yen amid global uncertainties does not bode well for corporate earnings.
Asia Pacific (ex Japan)	<ul style="list-style-type: none"> The recent trade truce between US and China was welcomed by the markets, however there is little confidence on how long this will hold. 	<ul style="list-style-type: none"> Economic growth over the quarter was largely subdued due to trade war tensions, impact of oil prices, Chinese slowdown and rising interest rates in a few economies.
Emerging Markets	<ul style="list-style-type: none"> At the G20 summit held in December, the US and China decided to hold new tariffs for 90 days, leaving room for discussions between the two parties. The optimism around the Brazilian market was restored after Jair Bolsonaro's victory. Markets expect his pro-business reforms could positively affect economic growth. 	<ul style="list-style-type: none"> The MSCI Emerging Markets Index ended the quarter lower, posting a negative return of 3.9% in sterling terms, in part due to lower growth forecasts emanating out from China.

Asset Class	What happened?	
	Positive Factors	Negative Factors
Conventional Gilts	<ul style="list-style-type: none"> The UK gilt yield curve marginally flattened further during the quarter with rates falling across all maturities. This was in part due to concerns over the rising prospects of a no-deal Brexit. Global factors also contributed to the fall in yields, notably the trade conflict between the US and China and the partial shutdown of the US government. Demand for gilts remains robust and auctions by the DMO continue to be oversubscribed. 	
Index-Linked Gilts	<ul style="list-style-type: none"> The yields on shorter dated index-linked gilts fell over the quarter, while those at the long end of the curve (over 30 years) remained broadly unchanged Demand for index-linked gilts remains robust and auctions by the DMO continue to be oversubscribed. 	
Corporate Bonds		<ul style="list-style-type: none"> UK corporate bonds generated negative returns over the quarter as corporate bond yields rose owing to wider credit spreads, while gilt yields fell. Across the various sectors, credit spreads widened with the capital goods sector being the worst performer over the quarter.
Commodities		<ul style="list-style-type: none"> The Bloomberg Commodity Index fell over the quarter, led by the fall in the prices of energy-related commodities, such as Brent crude oil and petroleum, on the back of rising production supply and concerns over slowing economic growth. Prices of industrial metals also fell due to the concerns over trade conflicts amidst a slowdown in the Chinese economy and global growth.
UK Property		<ul style="list-style-type: none"> UK house prices fell by 0.7% in December, falling by the most in monthly terms since July 2012. Overall, the UK construction sector ended 2018 on a negative note on the back of subdued demand for commercial projects and the growing risk of a no-deal Brexit.

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