AllenbridgeEpic
investment advisers

REPORT PREPARED FOR

London Borough of Islington Pension Fund

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1. Fund Manager Overview

Table 1 provides an overview of the external managers, in accordance with the Committee's terms of reference for monitoring managers.

Table 1

Manager	Departure of key individuals	Performance	Assets under management	Change in strategy/risk	Manager specific concerns
AllianzGI (RCM)	Five joiners and four leavers during the quarter.	Quarterly return broadly behind the Index by -1.3%. Outperforming over three years by +1.3% p.a. but still behind the target of +3.0% p.a.	£287 billion as at 31st December 2013 (latest published data.)		
Newton	Richard Wilmot, manager of the £1bn UK Equity Fund for Newton, has left the firm. No joiners this the quarter.	Outperformed the Index by +0.4% in the quarter. Also outperforming over three years by +1.1% per annum, but trailing the target of +2% p.a. Outperformance is attributable to successful stock selection.	£50.9 billion as at 30th June 2014, September figures not yet available.		
Standard Life	30 joiners and 14 leavers during the quarter. Craig Williamson, a Partner in SL Capital has retired after 12 years with the firm.	Over three years the Fund has outperformed by +1.1% p.a. and is now ahead of the performance target of +0.8% p.a.	Underlying fund has fallen in value by £138.6m this quarter. In two years the fund has dropped by £1 billion. £195.1 billion assets under management as at 30th June 2014.	Holding 6.1% in high yield non-benchmark bonds.	

Manager	Departure of key individuals	Performance	Assets under management	Change in strategy/risk	Manager specific concerns
Aviva	47 leavers and 63 joiners in Q3. 6 leavers and 8 joiners in real estate. Ian Womack, CEO of Real Estate, will be leaving the firm to pursue a new challenge.	Outperformed the benchmark by +2.3% p.a. over three years.	Fund was valued at £1.28 billion as at end Q3 2014.		
Thread-needle	Two new joiners and six leavers in Q3 2014. None of these was from the property team.	Outperformed the benchmark by +2.4% per annum over three years – ahead of their performance target.	£92.8 billion in assets worldwide as at 30th June 2014. Pooled fund has assets of £1.37 billion.		
Legal and General	Not reported.	Regional funds are all tracking the indices.	£465 billion of assets under management for over 3,000 clients worldwide as at end June 2013.		
Franklin Templeton	Not reported.	Another good quarter with a return of +9.0%. Beating the absolute return performance target of 10% p.a. by +25.7% over 12 months but trailing it by -2.6% over three years.			

Manager	Departure of key individuals	Performance	Assets under management	Change in strategy/risk	Manager specific concerns
Hearth-stone	Mark Witherspoon, Commercial Development Director, and Michael Blake, Interim Head of Finance, left the firm. Prakash Shar has replaced Michael Blake.	Ahead of the benchmark during the quarter by +1.1%, and behind by -1.4% for the twelve months to September 2014.	Fund was valued at £30.0m at end Q3 2014. Islington's holding represents 74% of the Fund.		

Key to shading in Table 1:

Minor concern

Monitoring required

2. Individual Manager Reviews

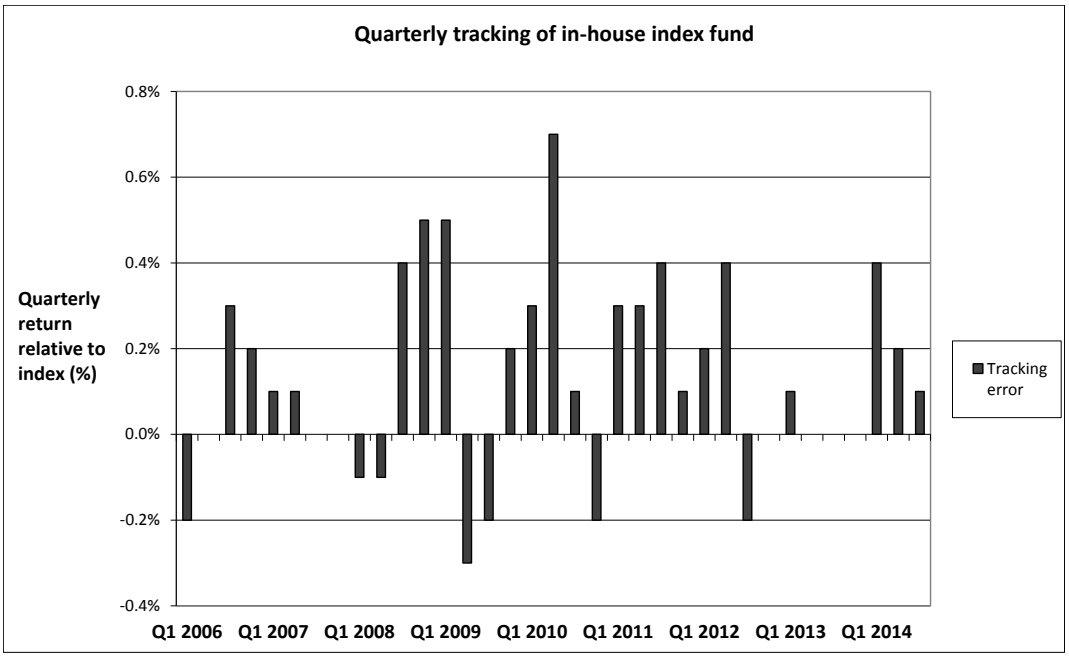
2.1. In-house – Passive UK Equities – FTSE All Share Index Fund

***Headline comments*:** The portfolio continues to meet its objectives. The fund delivered a quarterly return slightly ahead of the index benchmark (-0.9% versus -1.0%). Over three years the fund has outperformed the index by +0.4% p.a.

***Mandate summary*:** A UK equity index fund designed to match the total return on the UK FTSE All Share Index. The in-house manager uses Barra software to create a sampled portfolio whose risk/return characteristics match those of the index.

Performance attribution: Chart 1 shows the tracking error of the in-house index fund against the FTSE All Share Index since Q1 2006. **There are no performance issues.** Over three years, the small quarterly positive relative returns (shown in Chart 1) have accumulated, and as a result the portfolio has outperformed its benchmark by +0.4% per annum.

Chart 1



Source: AllenbridgeEpic based on WM figures

Portfolio risk: The tracking error on the portfolio as at end September was 0.21% per annum. In terms of sector bets, relative to the Index, the largest underweight sector position relative to the index was Financials (-0.8%). The fund was most overweight in Cyclical Services (+0.4%). This compares with sector bets of around 5-10% for the active managers.

Portfolio characteristics: The total number of holdings in the portfolio stood at 303 securities at the end of Q3 2014. There were £13 million of purchases across 150 securities, during the quarter, just after the Scottish Referendum, bringing the portfolio value to £322.2 million by the end of September.

2.2. AllianzGI (RCM) – Global Active Equities

Headline comments: In terms of relative performance, the fund had a poor quarter, trailing the index by -1.3%. Over three years the fund is outperforming by +1.3% per annum, however, mainly due to successful stock selection.

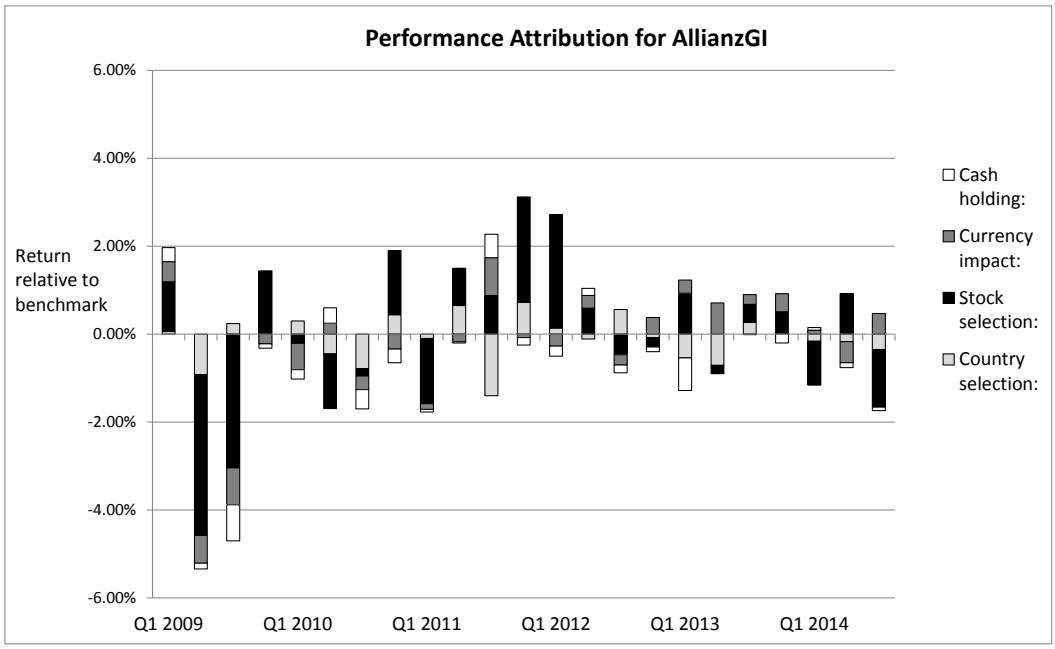
Mandate summary: An active global equity portfolio. AllianzGI operates a bottom-up global stock selection approach. They employ a team of research analysts to identify undervalued stocks in each geographical region (Europe, US, Asia Pacific). A global portfolio team is responsible for constructing the final portfolio. The objective of the fund is to outperform the FTSE All World Index by 3.0% per annum over rolling 3 year periods gross of fees.

Performance attribution: Chart 2 shows a breakdown of AllianzGI's quarterly performance since Q1 2009 relative to the benchmark.

Over the past three years, AllianzGI is ahead of its benchmark by +1.3% per annum, although **they are still trailing their performance target of 3% per annum**. Stock selection has made the biggest positive contribution over the past three years (+1.7% per annum). This is shown in the black bars in Chart 2 for each quarter. Currency selection has also made a positive contribution over three

years (+0.6% p.a.), but this has been offset by poor country bets (-0.1% p.a.) and by the cash holding (-0.5% p.a.)

Chart 2



Source: AllenbridgeEpic based on AllianzGI figures

Portfolio risk: In terms of sector bets, relative to the benchmark, the largest underweight sector position relative to the index is now Financials (-4.0%). The fund remains most overweight Industrials (+8.3%).

In terms of regional bets, the fund remains most overweight to Europe (+8.9% overweight). The largest underweight region is Emerging Markets (-5.3% underweight). The cash position stood at 3.6%.

Portfolio characteristics: The total number of holdings in the portfolio stood at 58 securities at the end of Q3 2014, within AllianzGI's normal range of 50-60 names. The beta on the portfolio was 0.99 at the end of September. This was a more defensive position than as at end June when the beta stood at 1.03.

Staff turnover: There were five joiners and four leavers during the quarter.

2.3. Newton – Global Active Equities

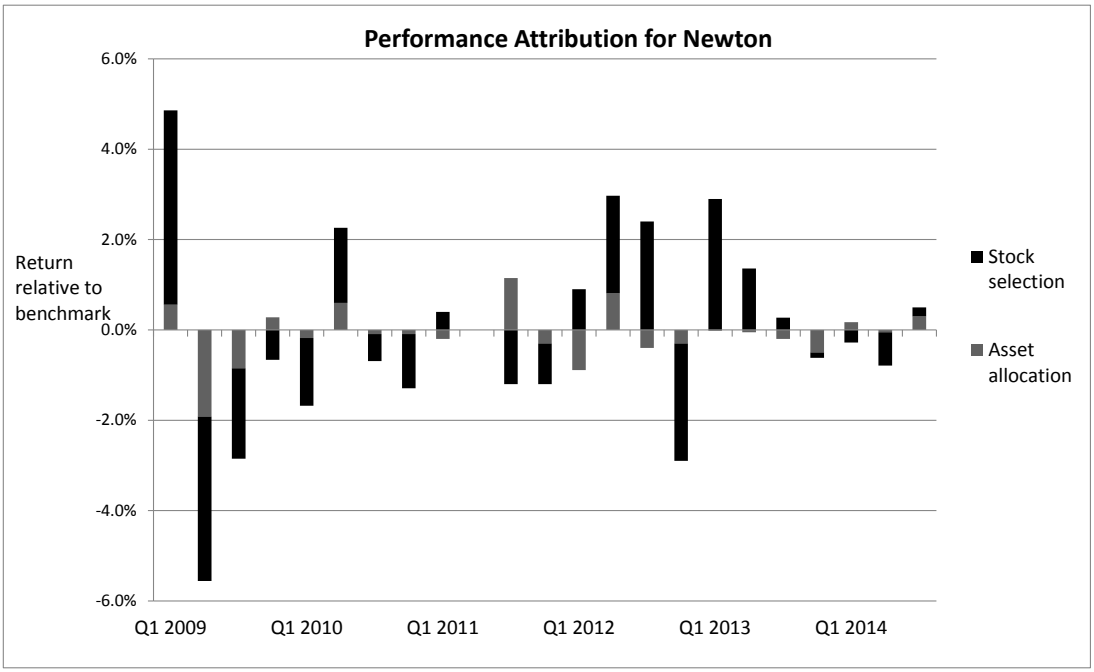
Headline comments: Newton were ahead by +0.4% during the quarter but the 12 month relative track record remains in negative territory at -1.3%. Over three years the picture looks better with outperformance of +1.1% per annum. This can be attributed to positive stock selection decisions (+1.8% p.a.) offset by negative asset allocation decisions (-0.5% p.a.). The fund's target performance is +2.0% per annum ahead of the benchmark.

Mandate summary: An active global equity portfolio. Newton operates a thematic approach based on 12 key themes that impact the economy and industry. Some are broad themes that apply over the longer term; others are cyclical. Stock selection is based on the industry analysts' thematic

recommendations. The objective of the fund is to outperform the FTSE All World Index by 2.0% per annum over rolling 3 year periods, net of fees.

Performance attribution: Chart 3 shows the attribution of relative performance between stock selection and asset allocation.

Chart 3



Source: AllenbridgeEpic based on Newton's performance attribution figures

Over the three years to September 2014, Newton was ahead of the benchmark, with a return of +17.0% p.a. compared to the index return of +15.7% p.a., an outperformance of +1.1% p.a. Stock selection accounted for +1.8% outperformance whilst asset allocation was negative (-0.5%). Note that the performance target is +2% p.a. outperformance over three years. **The fund is trailing its performance objective.**

In terms of stock and sector selection, during the quarter the most successful sector bet was Consumer Services (+0.5% contribution to relative performance) where Newton held an overweight position. The least successful sector was again Healthcare (-0.4% relative performance). Over the past 12 months, the Healthcare sector has detracted -0.9% from relative performance.

Portfolio Risk: The largest overweight regional allocation was in European Equities (+7.7% overweight). This has been a long-standing position that has been in place since Q3 2011. Successful stock selection in this region added +0.5% to relative performance during the quarter. The most underweight allocation remained Other Equities (-6.0%).

In terms of sector bets, Newton allocated more to the Healthcare sector during the quarter, making this the most overweight sector by quarter end (+8.5%). Note that this sector bet has detracted from performance over the past twelve months. The most underweight sector remained in Financials (-10.4%).

The level of active risk in the portfolio (i.e. the relative risk of the active bets being taken by Newton, or the tracking error) has increased to 2.7% as at quarter end, having dropped below the normal range of 2% and 6% last quarter. The concern with Newton's active risk is that too low a level will limit the manager's ability to meet the performance objective of +2% per annum outperformance a year over a three year period. It is certainly the case that relative returns are exhibiting more of a benchmark-hugging profile in the past twelve months, as shown in Chart 3.

Portfolio characteristics: At the end of Q3 2014, the portfolio held 80 securities (also 80 as at the end of Q2 2013). This at the lower end of Newton's expected range of between 80 and 120 stocks. Turnover over the past 12 months was 31%, at the low end of Newton's normal expected range of turnover to 30%-70%.

Staff turnover: during the quarter Richard Wilmot left the firm. He was the manager of Newton's £1 billion UK Equity Fund. He had previously been the manager of the £1.9 billion Higher Income Fund, but was replaced by Chris Metcalfe in March of this year.

Organisation: as at end June 2014, assets under management stood at £50.9 billion.

2.4. Standard Life – Fixed Income

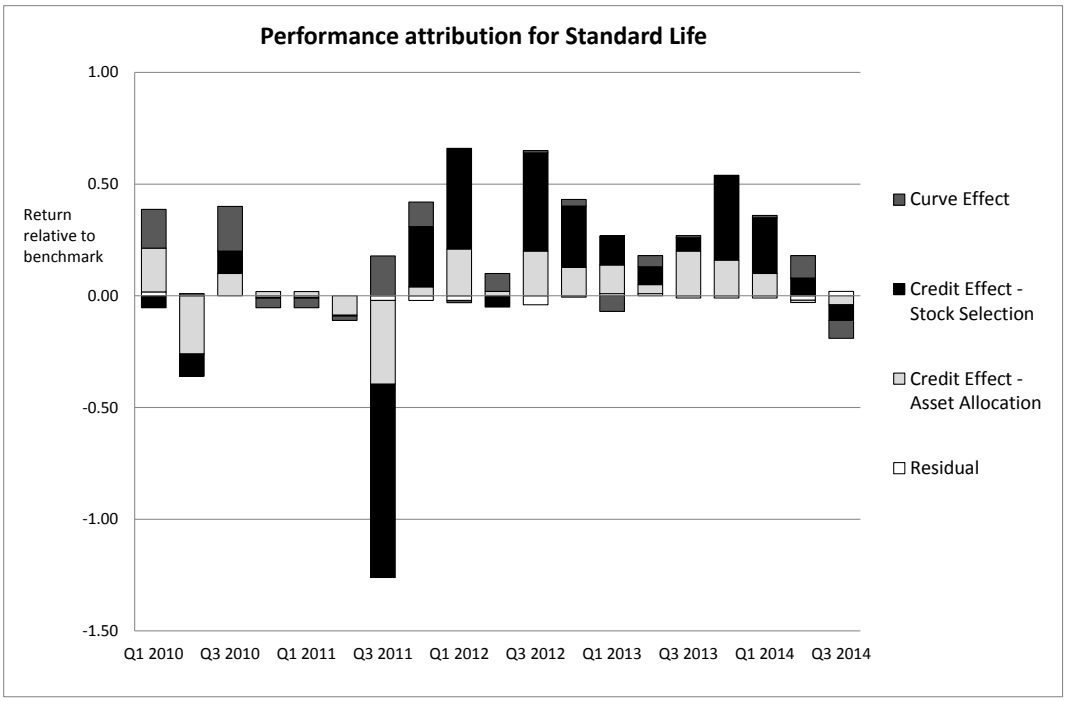
Headline comments: The portfolio was behind the benchmark during the quarter by -0.3%. Over three years, Standard Life's outperformance reached +1.1% per annum, so they are now ahead of their performance target of +0.8% per annum.

Mandate summary: An actively managed bond portfolio, invested in Standard Life's Corporate Bond Fund. The objective of the fund is to outperform the Merrill Lynch UK Non Gilt All Stocks Index by 0.8% per annum over rolling 3 year periods.

Performance attribution:

Chart 4 shows the performance attribution of the Corporate Bond Fund versus its benchmark. This is a pleasing profile for an active bond manager, with small but consistent levels of outperformance each quarter.

Chart 4



Source: AllenbridgeEpic based on Standard Life figures

Over three years, the portfolio has returned +9.1% p.a. compared to the benchmark return of +8.0% p.a., an outperformance of +1.1% p.a. Not only is this a very respectable absolute return, but the **fund is also meeting its performance objective of outperforming the benchmark by +0.8% per annum**.

The three year numbers have improved this quarter because the poor return in Q3 2011, when the portfolio underperformed its benchmark by -1.1%, has now dropped out of the three year figures.

Over the past three years, most of the outperformance has come from successful stock selection (+0.8%), with asset allocation contributing +0.4%.

Portfolio Risk: The largest holding in the portfolio at quarter end remains EIB 6% 2028 (2.0% of the portfolio). The largest overweight sector position remained Financials (+7.1%). The long-standing underweight position in sovereigns and sub-sovereigns remains (-15.9%). This position is at its highest level since inception.

The fund continues to hold 6.1% of the portfolio in non-investment grade bonds (these do not form part of the benchmark).

Portfolio characteristics: The value of Standard Life's total pooled fund at end September 2014 was £3,686.6 million, £138.6 million lower than at the end of Q2 2014. Over two years, the fund has fallen in value by £1,057.5 million. This reflects investors changing strategy and moving increasingly into absolute return bond strategies and/or multi asset credit. London Borough of Islington's holding of £204.9 million is now 5.6% of the total fund value. When Islington first invested, the percentage holding was 3.4%.

Staff turnover: There were 30 joiners during the quarter. These included Luke Powell, who has moved from Aviva to become a real estate specialist for Standard Life. There were 14 leavers during the quarter. This included Craig

Williamson, a Partner in the private equity arm, SL Capital. Craig has retired after 12 years with the firm. He was involved in the investment due diligence and selection of managers and co-investments. The SL Capital team is now 53 and there are 21 investment professionals.

2.5. Aviva Investors – Property – Lime Property Fund

Headline comments: The Fund underperformed the gilt benchmark by -3.0% during the quarter and underperformed the IPD Property Index return by -2.5%, as the property market continued to rally (the index has risen nearly 20% in the past 12 months). Over three years the Fund is ahead of its benchmark by +2.3%.

Mandate summary: An actively managed UK pooled property portfolio, the Lime Fund invests in a range of property assets including healthcare, education, libraries, offices and retail. The objective of the fund is to outperform a UK gilt benchmark, constructed of an equally weighted combination of the FTSE 5-15 Years Gilt Index and the FTSE 15 Years+ Gilt Index, by +1.5% per annum, over three year rolling periods.

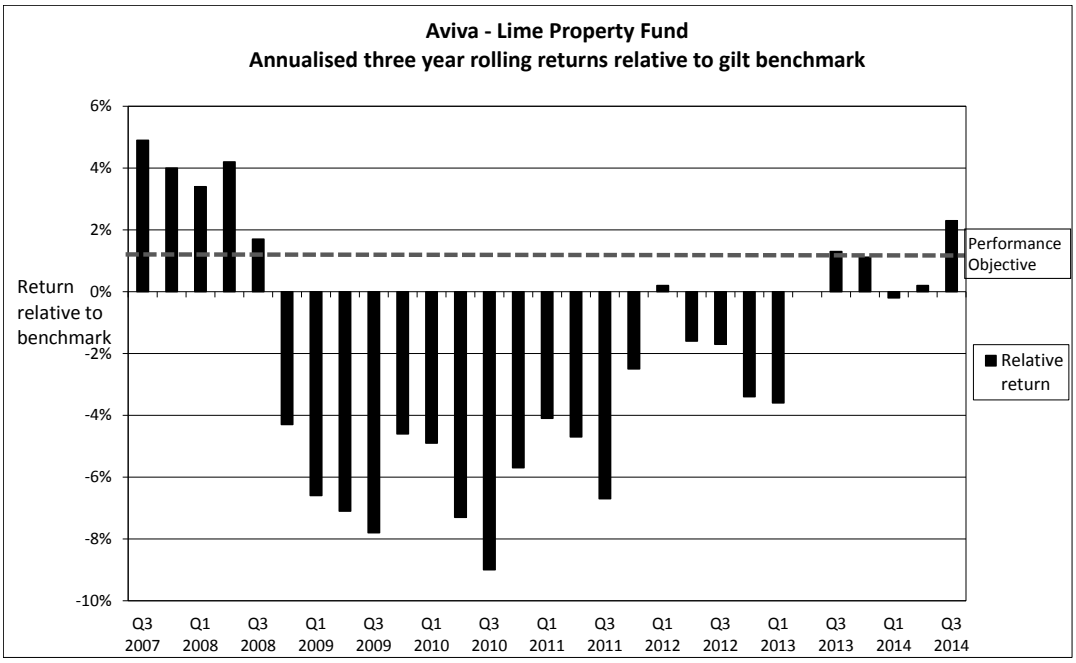
Performance attribution: The fund was behind the gilt benchmark this quarter by -3.0% although over the past twelve months it has outperformed by +0.8%. The portfolio trailed the IPD Index in Q3 2014 by -2.5% but in a strong property bull market this is to be expected with a low risk property portfolio such as the Lime Fund.

Over three years, the fund returned +7.1% p.a. compared to the gilt benchmark of +4.7% p.a., an outperformance of +2.3% per annum. The **portfolio is ahead of its performance objective of +1.5% per annum outperformance over three years**.

Of the +7.1% fund return over three years, 5.5% came from income, with the balance from capital gain. One of the key features of the Lime Fund is its positive exposure (currently over 80%) to fixed uplifts and RPI linked reviews.

Chart 5 shows the relative performance of the Fund compared to its gilt benchmark on a three year rolling basis.

Chart 5



Source: AllenbridgeEpic based on WM figures

Portfolio risk: The acquisition pipeline continued to grow during the quarter and the manager completed on two assets totalling £85 million. The average unexpired lease term is 20.5 years, with 10% of the portfolio's lease exposure in properties in over-35-year leases. 49% of the properties have public tenants with the largest sector exposure remaining supermarkets (22.6%). The cash allocation stood at 2.3% as at quarter end.

Portfolio characteristics: As at end June the Lime Fund was valued at £1.280 billion, an increase of £83.0 million from the previous quarter end. London Borough of Islington's holding represents 3.6% of the total Fund's value.

Staff turnover: this was a quarter of considerable staff turnover for Aviva. Across the whole firm, there were 47 leavers and 63 joiners. Of these there were six leavers and eight joiners within the real estate division. Four of the new joiners were infrastructure appointments. The Lime Fund team has not been impacted, however. At the end of the quarter, Aviva also announced that Ian Womack, CEO of the Global Real Estate division, would be leaving the firm to "pursue a new challenge". He had been at Aviva for 35 years. Ian will stay on at Aviva in order to appoint his successor which could be an internal or an external appointment. The executive team beneath Ian remains intact at this stage.

2.6. Threadneedle - Pooled Property Fund

Headline comments: The Fund's performance was +0.5% ahead of its benchmark (the IPD All Balanced – Weighted Average (PPFI) Index) during the quarter. Over three years, the Fund has outperformed its benchmark by +2.4% per annum. The Fund is ahead of its benchmark and beating the performance target of 1% p.a. above benchmark over three years.

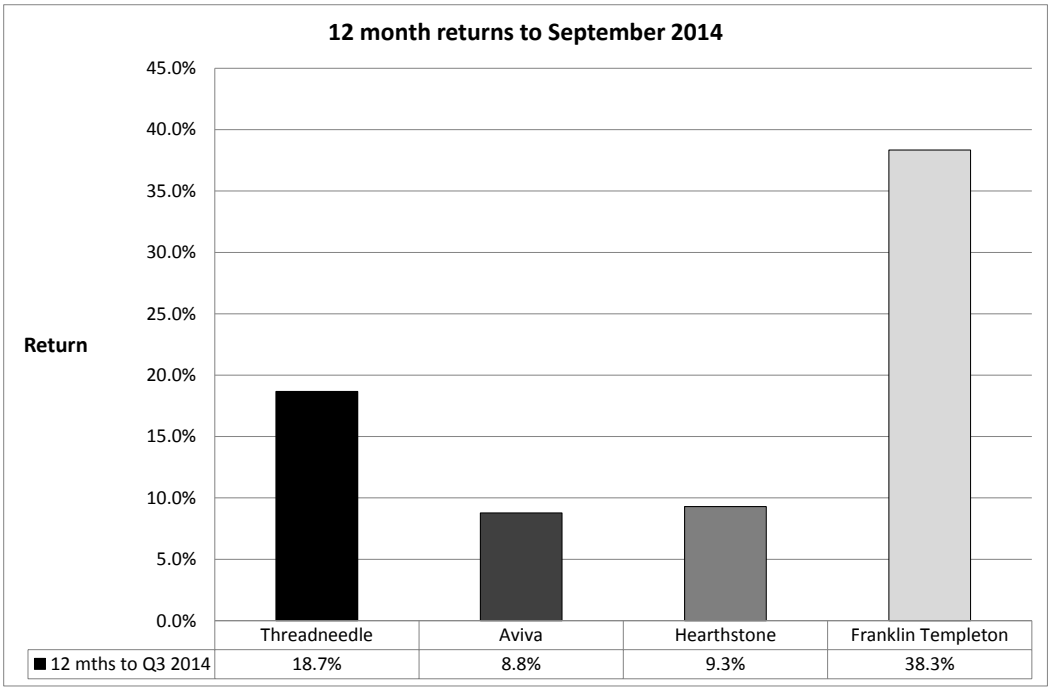
Mandate summary: An actively managed UK commercial property portfolio, the Threadneedle Pooled Property Fund invests in a diversified, multi-sector portfolio of UK property assets. Its performance objective is to outperform the AREF/IPD

All Balanced – Weighted Average (PPFI) Index by at least 1% p.a., net of fees, on a rolling three year basis. The benchmark changed at the end of Q4 2013. Prior to this, the benchmark was the CAPS pooled property median fund.

Performance attribution: The fund's outperformed the benchmark during the quarter by +0.5%. In terms of the three year performance, **the Fund is ahead of its benchmark and beating the performance target of outperforming by +1% per annum.** The portfolio returned +8.5% p.a. over three years compared with the benchmark return of +6.0% p.a.

Threadneedle ranked second across London Borough of Islington's property managers over the past 12 months. This is shown in Chart 6 which compares the returns for the four property managers.

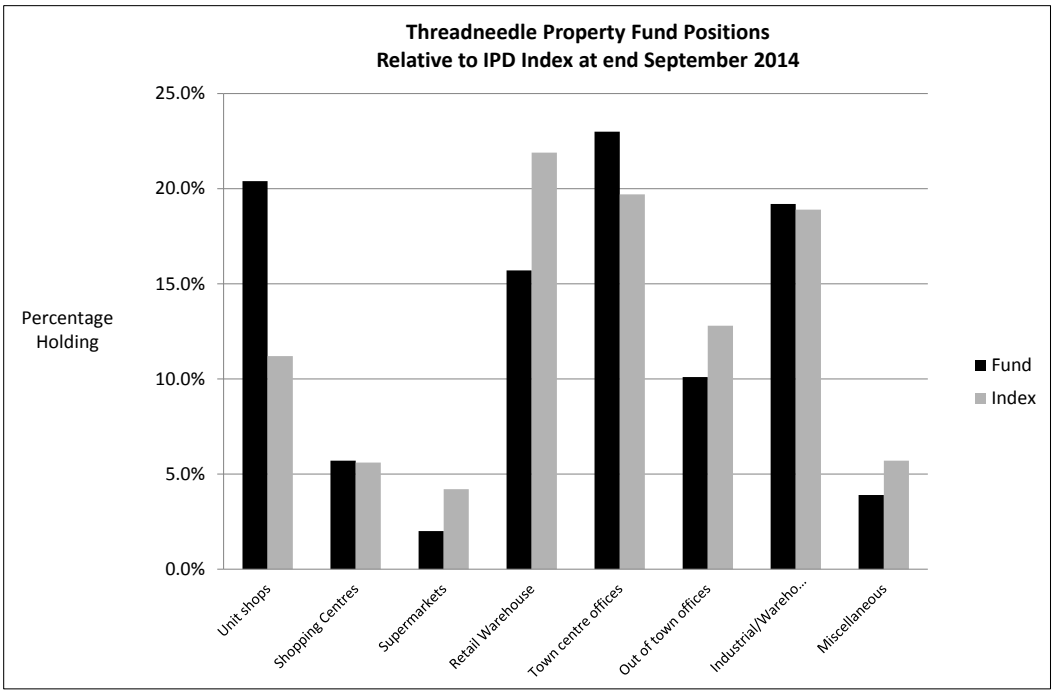
Chart 6



Source: AllenbridgeEpic based on WM data

Portfolio Risk: The fund did not make any new acquisitions in the third quarter of 2014. Chart 7 shows the current breakdown of the portfolio relative to its benchmark. However, across 48 rent reviews in the quarter, an additional £765,000 in rental uplift was a key success.

Chart 7



Source: AllenbridgeEpic based on Threadneedle data.

Portfolio characteristics: As at 30th September 2014, the Threadneedle Property Fund was valued at £1.37 billion, an increase of £65.2 million compared with June 2014. Over the past twelve months the fund has grown by £300 million. London Borough of Islington's investment represents 4.5%.

As at end September, the income yield on the fund stood at 6.5%, compared to 5.6% for the IPD Index. The fund had 251 properties and 1,083 tenancies. The top ten tenants form 22.4% of the total rent roll. The cash balance continues to be kept at a prudent level. As at end September it stood at 5.9%, well below the target maximum of 10%.

Staff turnover: there were six leavers and two joiners during Q3 2014, across the organisation. None of these was from the property division.

2.7. Legal and General Investment Management (LGIM) – Overseas Equity Index Funds

Headline comments: All the index funds were within the expected tracking range when compared with their respective benchmarks and there are no issues. The fundamental FTSE-RAFI Emerging Markets index fund underperformed its market capitalisation-weighted counterpart in Q3 2014 by -2.4%. For the 12 months to Q3 2014 the underperformance was -4.9%.

Mandate summary: Four regional overseas equity index funds, in Europe, Japan, Asia Pacific ex Japan, and emerging markets, designed to match the total return on the FTSE All World Regional Indices. One additional index fund is designed to match the total return on the FTSE-RAFI Emerging Markets Equity Index. The FTSE All World Indices are based on capitalisation weights whereas the FTSE-RAFI Index is based on fundamental factors.

Performance attribution: **The regional portfolios are all tracking their benchmarks**, as shown in Table 2.

Table 2

Q3 2014	Fund	Index	Tracking
Europe	-2.4%	-2.4%	0.0%
Japan	+3.1%	+3.1%	0.0%
Asia Pacific ex Japan	-0.6%	-0.7%	+0.1%
FTSE emerging markets	+3.1%	+3.1%	0.0%
RAFI emerging markets	+0.7%	+0.7%	0.0%

Source: LGIM

Portfolio Risk: The percentage allocation to each regional fund is based on pre-agreed band widths, which also take into account the global equity managers' allocations. The largest deviation from the benchmark allocation is North America which is 1.8% overweight.

2.8. Franklin Templeton – Global Property Fund

Headline comments: This is a long term investment and as such a longer term assessment of performance is recommended. The year to September 2014 was exceptionally good and the Fund return was +38.3% compared to its absolute return benchmark of 10% per annum. Over three years the performance numbers are improving and the fund has delivered a return of +7.1% per annum compared with the absolute return benchmark of 10% per annum.

Mandate summary: A global private real estate fund of funds investing in ten sub funds. The performance objective is an absolute return benchmark over the long term of 10% per annum.

Performance attribution: over the past twelve months, Franklin Templeton is the best performing fund across all four property managers, as shown in Chart 6. The fund is now entering its distribution phase and is performing well.

2.9. Hearthstone – UK Residential Property Fund

Headline comments: The portfolio returned +3.2% compared to the benchmark return of +2.0% for the quarter ending September 2014. Over 12 months the return was +9.3% compared to the benchmark return of +10.8%. Staff turnover remains on the high side for a small firm.

Mandate summary: The Fund invests in private rented sector housing across the UK and aims to outperform the LSL Acadametrics House Price Index (note that this excludes income), as well as providing an additional income return.

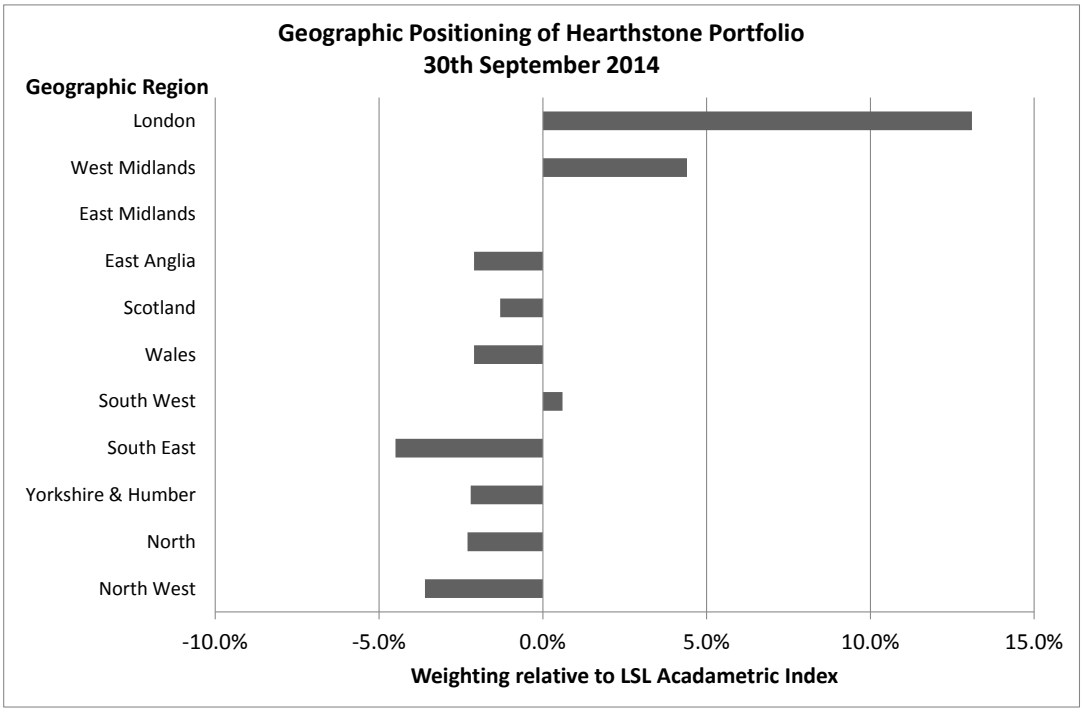
Performance attribution: The Fund returned +9.3% compared to the return on the index of 10.8% over the past 12 months. This places Hearthstone third out of four property managers in terms of returns over the past year (see Chart 6), slightly ahead of the Aviva Lime Fund. The yield on the portfolio was 5.4% at the end of September, after adjusting for voids.

Portfolio risk: The portfolio still holds a significant overweight position in London, relative to the benchmark. This is a consequence of an investment opportunity in Wembley. There were no acquisitions or disposals during Q3 2014, but the manager is looking to increase the underweight allocations in the South East, North West and the North. Hearthstone's normal strategy is to maintain broadly neutral regional bets in the portfolio.

As at end Q3 2014, the fund was valued at £30.0 million. London Borough of Islington remains the main investor, owning 71% of the total fund. Cash and liquid instruments in the portfolio stood at 10.7% at the end of Q3 2014, compared to a target level of 15%.

Portfolio characteristics: Chart 9 shows the regional bets in the portfolio. The biggest overweight region is London (+13.1%). The most underweight region relative to the index was the South East (-4.5%).

Chart 9



Source: AllenbridgeEpic based on Hearthstone figures

The Fund has a 21% allocation to detached houses, 52% allocated to flats, 22% in terraced accommodation and 5% in semi-detached.

Organisation and staff turnover: there were two leavers and two joiners during the quarter. Mark Witherspoon, Commercial Development Director, left although Hearthstone has indicated that he remains a non-Executive Director. The interim Head of Finance, Michael Blake, also left during the quarter and was replaced by Prakash Shar, also on an interim basis. The other joiner was Colleen Setchell, an Executive Assistant.

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12th November 2014