Essex County Council

Essex Pension Fund Investment Steering Committee

13:00	**Wednesday, 28 March 2018**	**Committee Room 1, County Hall, Chelmsford, CM1 1QH**

For information about the meeting please ask for:
Kevin McDonald, Director for Essex Pension Fund
Telephone: 01245 431301 (internal ext 21301) or 0333 0138 488
Email: kevin.mcdonald@essex.gov.uk

		Pages
1	**Membership, Apologies and Declarations of Interest** To note Membership, Apologies and any declarations of interest to be made by Members of the Committee during the meeting will be noted at this stage.	7 - 8
2	**Minutes of ISC meeting 21 February 2018** To approve as a correct record the Minutes of the Investment Steering Committee meeting held on 21 February 2018.	9 - 14

3	**Arrangements for future meetings** To agree a schedule of meetings for the municipal year 2018/19. The following dates have been proposed: <u>1pm start</u> 27 June 2018 18 July 2018 17 October 2018 28 November 2018 20 February 2019 27 March 2019	
4	**Treasury Management Strategy 2018/19** To consider a report by the Director for Essex Pension Fund	**15 - 50**
5	**Market Outlook and Background Q4 2017** To receive a report by Hymans Robertson	**51 - 68**
6	**Urgent Business** To consider any matter which in the opinion of the Chairman should be considered in public by reason of special circumstances (to be specified) as a matter of urgency.	
7	**Exclusion of the Public** To consider whether the public (including the press) should be excluded from the meeting during consideration of an agenda item on the grounds that it involves the likely disclosure of exempt information as specified in Part I of Schedule 12A of the Local Government Act 1972 (exclusion is recommended for the items set out in Part II below).	

Exempt Items

(During consideration of these items the meeting is not likely to be open to the press and public)

To consider whether the press and public should be excluded from the meeting during consideration of an agenda item on the grounds that it involves the likely disclosure of exempt information as specified in Part I of Schedule 12A of the Local Government Act 1972 or it being confidential for the purposes of Section 100A(2) of that Act.

In each case, Members are asked to decide whether, in all the circumstances, the public interest in maintaining the exemption (and discussing the matter in private) outweighs the public interest in disclosing the information.

8 Investment Tables: Quarter ended 31 December 2017

- Information relating to the financial or business affairs of any particular person (including the authority holding that information);

9 Training Session - Stock Lending

10 Stock Lending

- Information relating to the financial or business affairs of any particular person (including the authority holding that information);

11 Investment Strategy Review – Implementing the Transition from Equity to Alternatives Update

To consider a verbal update by Hymans Robertson in consultation with Independent Investment Adviser and the Director for Essex Pension Fund

12 Structural Reform of LGPS pooling quarterly JC update

- Information relating to the financial or business affairs of any particular person (including the authority holding that information);

13 Update on investment managers presenting: ISC Briefing note

- Information relating to the financial or business affairs of any particular person (including the authority holding that information);

14 **Investment Manager Presentation – Hamilton Lane**
To receive a presentation on the private equity portfolio from Hamilton Lane

15 **Urgent Exempt Business**
To consider in private any other matter which in the opinion of the Chairman should be considered by reason of special circumstances (to be specified) as a matter of urgency.

16 **Independent Investment Adviser (IIA) procurement**

- Information relating to the financial or business affairs of any particular person (including the authority holding that information);

17 **Date of Next Meeting**
To note the forthcoming meetings of the Investment Steering Committee and Essex Pension Fund Strategy Board.

Investment Steering Committee is on 27 June 2018 at 1pm, venue tbc

Essex Pension Fund Strategy Board is on 4 July 2018 at 1pm, venue tbc

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All Council and Committee Meetings are held in public unless the business is exempt in accordance with the requirements of the Local Government Act 1972. If there is exempted business, it will be clearly marked as an Exempt Item on the agenda and members of the public and any representatives of the media will be asked to leave the meeting room for that item.

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Agenda item 1

Committee: Essex Pension Fund Investment Steering Committee

Enquiries to: Samantha Andrews, Investment Manager

Membership, Apologies, Substitutions and Declarations of Interest

Recommendations:

To note

1. Membership as shown below
2. Apologies and substitutions
3. Declarations of interest to be made by Members in accordance with the Members' Code of Conduct

Membership
(Quorum: 4)

Membership	**Representing**
Councillor S Barker	Essex County Council (Chairman)
Councillor D Blackwell	Essex County Council
Councillor S Canning	Essex County Council
Councillor A Goggin	Essex County Council
Councillor A Hedley	Essex County Council
Councillor L Scordis	Essex County Council
Councillor C Souter	Essex County Council

Observers

Councillor C Riley	Castle Point District Council
Sandra Child	UNISON

Essex Pension Fund
Investment Steering Committee (ISC)

Minutes of a meeting of the Essex Pension Fund Investment Steering Committee held at 13:00pm at County Hall, Chelmsford on 21 February 2018

1 Membership

Present

Cllr S Barker (Chairman)	Essex CC
Cllr A Erskine (Conservative Group Substitute attending on behalf of Cllr S Canning)	Essex CC
Cllr A Goggin	Essex CC
Cllr A Hedley	Essex CC
Cllr M Maddocks (Conservative Group Substitute)	Essex CC
Cllr L Scordis*	Essex CC
Cllr C Souter	Essex CC

* Attended the meeting from 2pm

Sandra Child (Observer representing scheme employees)	UNISON

The following Advisers were present in support of the meeting;

Mark Stevens	Independent Adviser
John Dickson	Hymans Robertson
Matt Woodman	Hymans Robertson
Ian Colvin	Hymans Robertson

The following Officers were present in support of the meeting;

Kevin McDonald	Director for Essex Pension Fund
Samantha Andrews	Investment Manager

The following Essex Pension Fund Advisory Board (PAB) members were present as observers of the meeting:

Andrew Coburn	UNISON
Mark Paget	Active Member
Paul Hewitt	Deferred Member

2 Apologies for absence

Apologies were received from Cllr S Canning & Cllr D Blackwell (ECC Members) and Cllr C Riley (Castle Point District Council).

3 Declaration of Interest
Cllr Goggin declared that his wife and brother-in-law were in receipt of an Essex LGPS pension. Cllr Barker and Cllr Maddocks confirmed they are also in receipt of an Essex LGPS pension and Cllr Hedley declared he is in receipt of an Aviva Group pension.

4 Minutes
The revised minutes of the meeting of the Committee which took place on 21 November 2017 were approved as a correct record.

5 Matters of Interest
Kevin McDonald, Director for Essex Pension Fund highlighted a forthcoming conference that the Committee may wish to consider in attending: Baillie Gifford Long Term Global Growth half day Seminar on 24 May 2018.

It was noted that positive feedback had been received from Members who had attended this event in the past.

Members were asked to contact Officers by Friday 30 March 2018 if they were interested in attending either event.

The report was noted.

6 Market Background and Outlook Q4 2017
Matt Woodman from Hymans Robertson gave a verbal update on the markets since the Committees' last meeting in particular highlighting the short term volatility experienced in the markets over the last few weeks.

Following discussions the update was noted.

7 Urgent Part I Business
The Committee received a provisional schedule of meetings for the municipal year 2018/19.

27 June 2018
18 July 2018
17 October 2018
28 November 2018
20 February 2019
27 March 2019

It was agreed that all meetings will commence at 1pm and the schedule of dates was noted.

8 Exclusion of the public
(Press & Public excluded)

Resolved:

That the Public (including the press) be excluded from the meeting during consideration of the following items on the grounds that they involve the likely disclosure of exempt information as specified in Part 1 of Schedule 12A of the Local Government Act 1972:

- Passive Transition Update
- Review of Investment and Funding Objectives
- Review of Funds Costs
- Investment Manager Update – Officer & Adviser Briefing Note
- Introduction to the Investment Strategy Review
- Investment Manager Training Presentation – CBRE
- Investment Manager Presentation - Alcentra
- Investment Strategy Review– Implementing the transition from equity to alternatives
- Structural Reform of the Local Government Pension Scheme (LGPS) Pooling – AJC Quarterly update

9 Passive Transition Update
(Press & public excluded)

The Committee received a report from Kevin McDonald, Director for Essex Pension Fund and Samantha Andrews, Investment Manager updating Members on the timetable and implementation in relation to the transition of the passively managed assets and currency hedge arrangements from the incumbent Legal and General Investment Management (LGIM) to the new ACCESS single passive provider, UBS Asset Management (UBS).

The Committee noted:
- the passive portfolio transition timetable;
- the progress made to date in transitioning the passively managed assets from LGIM to UBS;
- the arrangements put in place to manage migration of the passive currency overlay with the new provider;
- that a further report be brought to a future meeting detailing the extent that the new currency overlay arrangement meets the Fund’s requirement; and
- that a further report detailing the total cost of the transition be brought to a future meeting.

10 Review of Investment and Funding Objectives
(Press & public excluded)

The Committee received a report from Ian Colvin, Independent Governance and Administration Adviser outlining the timetable agreed at the Essex Pension Fund Strategy Board (PSB) to undertake a fundamental review of the Funds objectives which would then be followed by an exercise to identify the risks that might hamper the successful attainment of those objectives. It was explained that prior to the PSB approving the full set of Fund objectives the ISC be given the opportunity to provide comment on the objectives specific to Investment and Funding.

It was **agreed that**:
- the investment objective “To ensure the Fund is properly managed” be amended to explicitly reference pooling and that a further amendment be made. The objective to now read *“To ensure the Fund’s investments is properly managed before, during and after pooling is implemented”;*
- the findings of the investment and funding objective review undertaken by the ISC be brought to the next PSB meeting; and
- the report be noted

11 Review of the Fund's Cost
(Press & public excluded)

The Committee received a report from Matt Woodman, Hymans Robertson summarising the independent review CEM Benchmarking had undertaken of the overall fees paid by the Fund, investment returns and net value added compared to its peers across the LGPS and global universal for the year to 31 March 2017.

It was **agreed that**:

- CEM undertake a cost benchmarking review as at 31 March 2018; and
- the report and conclusions be noted.

12 Investment Manager Update – Officer & Adviser Briefing Note
(Press & Public excluded)

The Committee received a report on the Officer & Adviser meetings held with both Aviva Investors and Stewart Investors. The report was noted.

13 Introduction to the Investment Strategy Review
(Press & Public excluded)

The Committee received a presentation from Matt Woodman outlining the key considerations in respect of implementing the target structure agreed in principle at the last meeting.

The presentation was noted.

14 Investment Manager Presentation – CBRE
(Press & Public excluded)

The Committee received a training presentation from Andrew Angeli, Achal Gandhi and Max Johnson from CBRE in respect of global property.

Following discussions the presentation was noted.

15 Investment Manager Presentation – Alcentra
(Press & Public excluded)

The Committee received a presentation from Simon Perry and Pascal Meysson from Alcentra, the Fund's Private lending manager.

Following discussions the presentation was noted.

16 Review of Investment Strategy – Implementing the transition from equity to alternatives
(Press & Public excluded)

The Committee received a presentation from Matt Woodman from Hymans Robertson outlining principles and considerations for the implementation of the target portfolio structure agreed in principle at the previous meeting.

It was **agreed that**:

- the recommendations set out on page 50 and 51 be agreed.

17 Structural Reform of Local Government Pension Scheme (LGPS) – Pooling AJC Update

(Press & public excluded)

Kevin McDonald, Director for Essex Pension Fund, gave an update outlining the latest developments in respect of the structural reform of the LGPS.

The progress on the Operator procurement and implementation, sub fund construction, ACCESS Governance review, client function and support arrangements workstreams were outlined.

Members were informed of the conclusion of the Operator procurement and the award of the contract to the preferred bidder. It was explained that further progress had also been made on the initial sub fund seeding arrangements.

Members noted that Muse Advisory Ltd had been appointed to assist with the review and development of ACCESS governance arrangements in particular assisting with defining roles & responsibilities and to advise on overlaps and potential gaps, in accordance with accepted best governance practice.

The update was noted.

18 Urgent Exempt Business

(Press & public excluded)

There were none.

There being no further business, the meeting closed at 4.35pm

Chairman
28 March 2018

Investment Steering Committee	AGENDA ITEM 4
date: 28 March 2018	

Essex Pension Fund Treasury Management Strategy 2018/19

Report by the Director for Essex Pension Fund
Enquiries to Kevin McDonald on 0333 0138 488

1. Purpose of the Report

1.1 To present the 2018/19 Essex Pension Fund Treasury Management Strategy.

2. Recommendation

2.1 That the 2018/19 Essex Pension Fund Treasury Management Strategy be approved.

3. Background

3.1 The Treasury Management Code issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) requires an annual Treasury Management Strategy to be agreed. The attached Treasury Management Strategy for the Essex Pension Fund has been prepared having regard to the Treasury Management Code and informal guidance issued by the DCLG.

4. Essex Pension Fund Treasury Management Strategy

4.1 The 2018/19 Treasury Management Strategy for the Essex Pension Fund replicates to a large extent the Treasury Management Strategy already approved for Essex County Council, but has been adapted to reflect the limited borrowing requirements, use of global custodian and the separate governance arrangements of the Pension Fund.

4.2 Tracked additions are highlighted in coloured text and deletions highlighted in strikethrough ~~coloured text.~~

4.3 The Fund's global custodian is Northern Trust. The principles of the custodian cash management arrangements are highlighted in Section B of the attached strategy. Furthermore a series of questions highlighting operational aspects of the custodian cash management arrangements form Annex 2 of the attached strategy.

4.4 Section C, Cashflow Management Arrangements has been updated to reflect the revised Finance Schedule, attached at appendix 1. The forecast for 2018/19 predicts a shortfall of £27m this is offset by the net positive cashflow received in 2017/18.

5. Background Papers

5.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

5.2 Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (the Treasury Management Code) issued by CIPFA.

5.3 Northern Trust Global Funds PLC prospectus June 2017.

5.4 BNP Paribas Insticash prospectus December 2017.

5.5 Finance Schedule updated March 2017

Appendix 1

Finance Schedule

		2016/17 actual £ (000)	2017/18 estimate £ (000)	2018/19 forecast £ (000)
EXPENDITURE	Retirement Pensions	183,131	188,565	197,993
	Retirement Lump Sums	36,481	35,843	36,560
	Death Benefits	5,693	5,322	6,121
	Leavers benefits	12,948	13,062	13,715
	Expenses	2,580	2,900	3,058
	Pooling expenses	80	90	250
TOTAL		**240,913**	**245,782**	**257,696**
INCOME	Employees Contributions	54,497	55,138	56,517
	Employers Contributions			
	Ongoing	116,907	137,289	138,865
	Deficit	48,616	63,831	19,407
	Financial Strain	4,339	3,133	2,800
	Transfer Values in	12,465	11,568	11,684
	Other income	1,720	1,787	1,876
TOTAL		**238,544**	**272,746**	**231,149**
Net cash flow excl. Investment Income		**(2,369)**	**26,964**	**(26,547)**

Essex Pension Fund

Treasury Management Strategy for ~~2017~~2018/~~18~~19

Investment Steering Committee ~~4 April 2017~~28 March 2018

Introduction

The treasury management activities covered by this document are comprised of three separate areas:

Section A

- The day to day management of the Pension Fund's cash flows and associated short term cash investments known as "In house cash". These activities are undertaken by Essex County Council on behalf of the Pension Fund under a service level agreement.

Section B

- The cash held and managed by the Global Custodian as part of the Fund's investment strategy.

Longer term investments are administered separately by external fund managers and these activities are covered in the Pension Fund Statement of Investment Principles agreed by the Investment Steering Committee each year.

Section C

- The requirement to realise investment income in order to meet a shortfall in income to meet a proportion of future benefit payments.

Section A – "In House Cash" Treasury Management Arrangements

In undertaking the treasury management activities for the Essex Pension Fund, in the absence of any specific guidance on treasury management for Local Government Pension Scheme funds, Essex County Council will comply with the Treasury Management in the Public Services: Code of Practice and Cross-Sectorial Guidance Notes (the Treasury Management Code) issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

A fundamental aim of treasury management is to effectively control the risks associated with treasury management activities and to pursue value for money, in so far as this is consistent with the effective management of risk.

The Treasury Management Code requires the following:

- A **Policy Statement** which states treasury management policies, objectives and approach to risk management.
- **Treasury Management Practices** (TMPs) which set out the manner in which the organisation will seek to achieve those policies and objectives, and prescribe how these activities will be managed and controlled.
- An annual **Treasury Management Strategy** that outlines the expected treasury activity. The strategy must define the organisation's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The Policy Statement and TMP's were updated and approved by the Board in March 2010. As no further changes or updates are considered necessary, neither have been reproduced in this report.

Treasury Management Strategy

The Treasury Management Strategy is set out in the subsequent paragraphs.

Short Term Cash Investment Strategy

- **Key objectives**
  The primary objectives of investment activities are:
  - Firstly, to **safeguard** the principal sums invested;
  - Secondly, to ensure adequate **liquidity**; and
  - Lastly, to consider investment returns or **yield**.

Surplus cash balances will only be invested on a short term basis (up to a maximum period of 364 days) until the funds are next required. Longer term investments are outside the scope of this document.

- **Investment counterparty selection criteria**

  Funds will be invested according to the Secretary of State's definition of specified investments, these being sterling deposits made for periods of less than one year, offering high security and high liquidity. Specified investments may include deposits with the UK Government, other local authorities, money market funds and bodies of high credit quality.

  A lending list will be compiled to include counterparties satisfying the criteria set out within **Annex 1**. The lending limits that will be applied to counterparties satisfying these criteria are also set out within **Annex 1**. Additional operational market information (e.g. Credit Default Swaps, negative rating watches/outlooks) will also be considered before making any specific investment decisions.

  The criteria for choosing counterparties provide a sound approach to investment in normal market circumstances. However, the Executive Director for Corporate and Customer Services will determine the extent to which the criteria set out within **Annex 1** will be applied in practice (i.e. according to prevailing market circumstances).

- **Liquidity**

  Liquidity is defined as having adequate, but not excessive cash resources, borrowing arrangements and overdraft or standby facilities to ensure that funds are available, at all times, for the achievement of the Pension Fund's objectives. In this respect, the Pension Fund will seek to maintain a contingency of at least **£1m** of cash available with a week's notice. This will be in excess of amounts available at short notice for managing expected cash flows.

- **Performance**

  Investment performance will be measured against the 7 Day London Interbank Bid Rate (LIBID); the aim being to achieve investment returns that are equivalent to, or greater than, the average 7 Day LIBID rate for the year (i.e. subject to security and liquidity considerations being fully satisfied).

Interest Rates

An estimate of the movement in interest rates over the forthcoming three years is provided below :-

Expected movement in interest rates	~~2016-17 latest estimate~~	2017-18 Latest Estimate	2018-19 Estimate	2019-20 Estimate	2020-21 Estimate
Bank rate (at each 31 March) Source : ~~Capita~~ Link Asset Services (February 20~~17~~18)	~~0.25%~~	~~0.25~~0.50%	~~0.25~~1.00%	~~0.75~~1.25%	1.50%

The estimated average balance for "In house cash" is around **£20m**. A **1%** movement in interest rates would affect the level of income earned from short term investments by **£200,000**.

Given the short term nature of "In house cash", no limits are proposed on the maximum exposure to fixed or variable rates of interest.

Borrowing

The administering authority does not have the power to borrow on behalf of the Pension Fund, other than temporary borrowing for the following specific purposes detailed in section 5 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 :-

- paying benefits due under the Scheme, or
- to meet investment commitments arising from the implementation of a decision by the Fund to change the balance between different types of investment.

In the context of this Strategy, short term borrowing will only be undertaken in exceptional circumstance to manage unexpected cash flow fluctuations which occur as a result of the above circumstances.

If short term borrowing is necessary, this will be secured via an overdraft facility with the Fund's bankers or by borrowing from the money markets or other local authorities.

Treasury Management Advisors

Essex County Council currently employs **~~Capita~~ Link Asset Services** (Treasury Solutions) as its treasury management advisor.

~~Capita~~ Link Asset Services provide a range of services, including technical advice on treasury matters, economic and interest rate analysis and credit worthiness information. Notwithstanding this, the final decision on treasury matters remains vested with the Essex Pension Fund Investment Steering Committee, and for day to day treasury management, with the Executive Director for Corporate and Customer Services.

The services received from the Treasury Management Advisors are subject to regular review.

Section B – Custodian Cash Management Arrangements

One of the functions provided by the Fund's custodian, Northern Trust, is a banking service. A separate bank account is set up in each currency required by each mandate. At 1 March the Fund held £ ~~114.6~~139.5m in cash at the custodian. The details are set out in the table below.

01-Mar-17	£m	%
Sterling	86	75%
Dollar	21.6	19%
Euro	4.8	4%
Other	2.2	2%
	114.6	100%

01-Mar-18	£m	%
Sterling	79.6	57%
Dollar	49.1	35%
Euro	9.8	7%
Other	1.0	1%
	139.5	100%

If no other action were taken, these monies would remain on deposit with Northern Trust earning interest at the Custodian's rates.

However, in order to maximise the interest earned where possible, a "cash sweep" is in place for amounts held in sterling and US dollar. This ensures that balances (not required to settle trades) in these currencies across the Funds are swept each day into Global Liquidity Funds (GLFs) managed by either BNP Paribas Investment Partners UK Limited or Northern Trust Global Funds PLC where they earn a higher rate of interest. The three currencies subject to the sweep typically constitute in excess of 95% of all custodian cash balances.

The Fund is also able to utilise the Euro GLF sweep, however due to its adoption of negative interest rates in May 2015 this facility is not currently in use. The GLF vehicles used have obtained, and seek to maintain an Aaa/Mf+ rating from Moody's and an AAA rating from Standard & Poor's. The GLFs operates a soft limit of 10% in any single security, although there are circumstances in which higher holding levels are permitted. A listing of the investment restrictions for both the Northern Trust GLFs and BNP Paribas GLFs are shown are shown in **Annex 3.1** and **3.2.**

The GLFs are open-ended collective investment companies (OEIC). This means that in placing monies in the GLFs via the cash sweep, the Essex Pension Fund becomes a shareholder and has a share in the pool of investments. A GLF must appoint a board of directors, an investment manager, an administrator and custodian. Clients invest, not with the fund manager, but in the fund run by the fund manager. The manager manages the investments of the fund, an administrator runs the back office and the assets are kept in safe-keeping for the fund by the custodian. The GLFs' overall ratings have two components: a credit risk rating (normally AAA) and a market risk rating. To achieve and maintain the rating, the funds must meet rigorous standards on investment quality, diversification and liquidity profile. Both internal management and the rating agencies ensure compliance with regulatory, prudential, investment and credit policy guidelines. The processes are monitored further by administrators, custodians and auditors.

In order to limit the exposure of the Fund to any single financial institution a maximum limit is set for both the Northern Trust and BNP Paribas GLFs.

A series of detailed questions on the how the GLFs operate in practice are shown in **Annex 2** of this document.

Impact of lump sum deficit contributions and income realisation

In addition to the working balances of the investment managers, cash management arrangements now need to accommodate the impact of lump sum deficit payments and income realisation.

Under the terms of the current Funding Strategy, it is possible for certain fund employers to opt to pay deficit "up front" in April (rather than the traditional 12 monthly instalments). Furthermore, as highlighted in Section C, it is forecast that some investment income will need to be used rather than automatically reinvested in order to finance part of the Fund's benefit expenditure from ~~2017/18~~ 2018/19.

As a consequence the GLFs will be used in order to allow the most effective management of monies immediately prior to being allocated to fund managers or directed to pay benefits.

GLF Limits

~~Revised employer contribution rates are payable from April 2017 owing to the outcomes of the 2016 triennial actuarial valuation. In line with the Funding Strategy agreed by the Pension Strategy Board on 8 March 2017, a number of non-pooled employers were offered a series of options which included up front annual and triennial deficit repayments. Twelve of the seventeen major tax raising bodies have chosen to make a triennial deficit payment in April 2017 which in turn is the major reason behind estimated deficit income of over £60m due in that month.~~

As its meeting of 21 February 2018 the ISC agreed principles in respect of any reallocation of equities to the alternative and bond mandates. It was agreed that up to 1% of the Fund's assets can be held in cash (separate to that the managers may hold for efficient portfolio management) in expectation of a drawdown notice or other cash flow requirement for the Fund.

The limits for ~~2017/18~~ 2018/19 are set out below and reflect an ~~temporary~~ increase for both the Northern Trust GLF and BNP Paribas GLF ~~at the start of the year~~ to reflect the circumstances outlined above:

~~Northern Trust GLF - £140m (April & May 2017)~~

Northern Trust GLF - £80m (no change on an operational basis)~~remainder of year and in line with 2016/17~~)

Northern Trust GLF - £150m (on a temporary basis to facilitate the redeployment of assets)

BNP Paribas GLF - £60m (no change on an operational basis)

BNP Paribas GLF - £130m (on a temporary basis to facilitate the redeployment of assets)

Section C – Cashflow Management Arrangements

The Fund is maturing and analysis has been undertaken to forecast when new contributions (employees and employers including deficit) are not enough to meet all benefit payments falling due. This is normal for a pension scheme and reflects the purpose of the Fund (accumulate monies and then pay it out in benefits).

The current position is that the Fund is broadly cash neutral, with ~~modest~~ differences between the income and expenditure in the years analysed in the table below.

Table: Fund cashflow forecast

	~~2015/16 actual £'000~~	~~2016/17 estimate £'000~~	~~2017/18 forecast £'000~~
~~Expenditure: benefits, transfers out and expenses~~	~~224,037~~	~~233,160~~	~~256,687~~
~~Income: employee/employer contributions and transfers in~~	~~230,638~~	~~229,617~~	~~262,555~~
~~Net cashflow excl. investment income: positive / (negative)~~	~~6,601~~	~~(3,544)~~	~~5,867~~

	2016/17 actual £ (000)	2017/18 estimate £ (000)	2018/19 forecast £ (000)
Expenditure (benefits, transfers out and expenses)	**240,913**	**245,782**	**257,696**
Income (ongoing contributions, deficit contributions and transfers in)	**238,544**	**272,746**	**231,149**
Net cashflow excl. Investment Income	**(2,369)**	**26,964**	**(26,547)**

The cashflow forecast will be subject to regular periodic review.

Income Realisation Strategy

In order to meet the short to medium term cashflow requirements, the Investment Steering Committee at its 23 February 2015 meeting agreed to realise income from L&G's UK assets and Aviva property portfolio.

Realised income may be held in cash short term in order to meet a proportion of benefit payments.

The income realisation strategy will be subject to regular periodic review.

Counterparty Criteria for Investments – In House Cash **Annex 1**

Lending List

The Pension Fund will only invest its short term funds with UK banks and building societies, and non UK banks domiciled in a country with a minimum sovereign long term rating of **AA**, that have credit ratings equivalent to or better than the following:

Rating category	Credit rating agencies		
	Fitch	Standard and Poor	Moody's
Short term rating	**F1**	**A-1**	**P-1**
Long term rating	**A**	**A**	**A2**

The above ratings will be used to determine the pool of counterparties with whom the Pension Fund can transact. Where the counterparty is rated by more than one credit rating agency, the lowest ratings will be used to determine whether or not it is included on the counterparty list. However, financial institutions will only be considered for inclusion if they have a credit rating in both of the rating categories.

The criteria outlined above will ensure that funds are only invested with high quality counterparties. The short and long term ratings will be used to determine the maximum amount that can be invested with each of these counterparties, and for what period – see lending limits section.

In addition, the Pension Fund may invest its funds with:

- The UK Government.
- Other local authorities.
- Pooled investment vehicles (i.e. Money Market Funds) that have been awarded an **AAA** credit rating.
- Financial institutions fully or part nationalised by the UK Government whose credit ratings do not meet the above criteria.
- Bank subsidiaries and treasury operations which do not have a full set of credit ratings, provided the parent bank has the necessary ratings outlined above. In addition, the subsidiary must itself have a short and long term rating meeting the above criteria or have an unconditional guarantee from the parent bank.

In the event that the Pension Fund's own banker falls below the minimum credit rating criteria outlined above, and is not nationalised or part nationalised, the bank will be used for transactional purposes only, and not as an active outlet for investments.

Notes:

- There are three main credit rating agencies that assign ratings to financial institutions, namely Fitch, Standard and Poor and Moody's. When these agencies assign ratings, they take account of any country specific circumstances. Ratings are therefore applicable worldwide; hence the risk of investing with two different counterparties that have similar ratings is the same, irrespective of their country of origin.
- Definitions of the credit ratings of the three main credit rating agencies are summarised in Annex 2. Full details are available upon request.
- Credit ratings are continually monitored, with changes in credit ratings being notified by the Council's treasury management advisors. Counterparties will be removed from the Pension Fund's lending list in the event that they receive a downgrading to their credit rating status below the minimum criteria outlined above.
- Counterparties that are placed on 'negative ratings watch' will remain on the Pension Fund's lending list at the discretion of the Executive Director for Corporate and Customer Services, in consultation with the Chairman of the Pension Fund Board (or Deputy Chairman of the Pension Fund Board if the Chairman is unavailable).
- Money Market Funds (MMFs) are short term pooled investments that are placed, by a manager, in a wide range of money market instruments. The size of the investment pool of a MMF enables the manager to not only offer the flexibility of overnight and call money, but also the stability and returns of longer dated deposits. Strict rules and criteria are set down by the official rating agencies, covering the types of investment counterparties used, the maturity distribution of the funds and investment concentrations. The MMFs that the Pension Fund uses will be denominated in sterling and be regulated within the EU.

Lending Limits

For banks and building societies satisfying the 'lending list' criteria, lending limits will be determined with reference to the counterparties' short and long term credit ratings, as follows:

- Investment limit of **£7.5m** for investments of up to **1** year:

Rating category	Credit rating agencies		
	Fitch	Standard and Poor	Moody's
Short term rating	F1+	A-1+	P-1
Long term rating	AA-	AA-	Aa3

- Investment limit of **£5m** for investments of up to **1** year:

Rating category	Credit rating agencies		
	Fitch	Standard and Poor	Moody's
Short term rating	F1	A-1	P-1
Long term rating	A	A	A2

Lending limits for other counterparties will be as follows:

- No restrictions will be placed on the amounts that can be invested with the UK Government (i.e. Debt Management Office). It is not possible to set up a separate Pension Fund account with the DMO so funds would be placed via the County Council, although the credit risk would remain with the Pension Fund.
- An investment limit of **£10m** will be applied for investments of up to **one** year with individual Money Market Funds.
- An investment limit of **£7.5m** will be applied for investments of up to **one** year with individual top tier local authorities. Top tier local authorities will include county councils, unitary and metropolitan authorities and London boroughs.
- An investment limit of **£5m** will be applied for investments of up to **one** year with individual lower tier local authorities. Lower tier local authorities will include district / borough councils, and police and fire authorities.
- In addition to the limits outlined above, a further restriction will be applied in respect of investments with non UK financial institutions; that is, a country limit of **£5m** will be applied. The country limit will restrict the total amount that can be invested within any one country outside of the UK at any one time.

Current Institutional Lending List

Counterparty ESSEX PENSION FUND	Investment limit £m	Maximum duration
UK BANKS		
HSBC		
HSBC Group limit	7.5	
HSBC - fixed term	7.5	364 days
HSBC - BIBCA (call account)	7.5	call
Lloyds Banking Group		
Lloyds Group limit	5	
Lloyds TSB Bank - fixed term	5	364 days
Lloyds TSB current account	5	call
Royal Bank of Scotland		
RBS Group Limit	5	
RBS - fixed term	5	364 days
RBS - CALL account	5	call
Santander UK		
Santander Group Limit	5	
Santander - CALL account	5	364 days
UK BUILDING SOCIETIES		
Nationwide	5	6 mnths
FOREIGN BANKS (Country limit £5m)		
Australia		
Commonwealth Bank of Australia	5	364 days
Canada		
Bank of Montreal	5	364 days
Bank of Novia Scotia	5	364 days
Netherlands		
Rabobank	5	364 days
Singapore		
Development Bank of Singapore	5	364 days
Overseas Chinese Banking Corporation	5	364 days
Sweden		
Svenska Handelsbanken - call a/c	5	call
OTHER		
Money Market Funds		
Standard MMFs (limit £20m)	20	
Black Rock - Inst. Sterling Liquidity	10	364 days
Standard Life - Sterling Liquidity Fund	10	364 days
LOCAL AUTHORITIES		
Top Tier Local Authorities	7.5	364 days
- [Name of Authority]	7.5	364 days
Lower Tier Local Authorities	5	364 days
- [Name of Authority]	5	364 days

Counterparty ESSEX PENSION FUND	Investment limit £m	Maximum duration
UK BANKS		
Barclays Bank		
Barclays Group limit	5.00	
Barclays - CALL acct	5.00	call
HSBC		
HSBC Group limit	7.50	
HSBC - BIBCA (call account)	7.50	call
Lloyds Banking Group		
Lloyds Group limit	5.00	
Lloyds current account	5.00	call
Royal Bank of Scotland		
RBS Group Limit	5.00	
RBS - CALL account	5.00	call
Santander UK		
Santander Group Limit	5.00	
Santander - CALL account	5.00	call
UK BUILDING SOCIETIES		
Nationwide	5.00	6 mnths
FOREIGN BANKS (Country limit £5m)		
Sweden		
Total country limit	5.00	364 days
Svenska Handelsbanken - call a/c	5.00	call
OTHER		
Money Market Funds		
Standard MMFs (limit £20m)	20.00	
Black Rock - Inst. Sterling Liquidity	10.00	364 days
Standard Life - Sterling Liquidity Fun	10.00	364 days
LOCAL AUTHORITIES		
Top Tier Local Authorities	7.50	
- [Name of Authority]	7.50	364 days
Lower Tier Local Authorities	5.00	
- [Name of Authority]	5.00	364 days

Annex 2

Pension Fund Treasury Management
Custodian Cash Balances Arrangements

A number of *questions* are set and answered within this note, and the questions are grouped into four sections:

1. Background
2. Risk Management
3. Interest
4. Ratings

1. Background

The Pension Fund's Global Custodian is Northern Trust. Details of the Fund's cash balances held at the Custodian as at 1 March 2018 are set out below.

01-Mar-18	£m	%
Sterling	79.6	57%
Dollar	49.1	35%
Euro	9.8	7%
Other	1.0	1%
	139.5	100%

How is this cash managed?
Sterling: Sterling cash balances are swept into the (sterling) Northern Trust GLF and the BNP Paribas Insticash Fund.
Dollar: Dollar balances are swept into the (dollar) Northern Trust GLF and the BNP Paribas Insticash Fund.
Euro: The Fund is also able to utilise the Euro GLF sweep, however due to its adoption of negative interest rates in May 2015 this facility is not currently in use.

As a consequence, the Fund's cash is placed in a total of four separate sub funds.

How are GLFs constituted?
The GLFs are established as Investment Companies qualifying under the terms of the European Undertakings for Collective Investments in Transferable Securities (UCITS) Regulations/Directives. The BNP Paribas GLF is incorporated in Luxembourg and Northern Trust Global Fund is incorporated in Ireland.

What are the objectives?
The investment objective of the funds is to maximise current income to the extent consistent with the preservation of capital and maintenance of liquidity by investing in a range of high quality fixed and adjustable rate instruments.

Are the GLFs actively managed?
Yes.

How do the GLFs invest?
The Funds allow for investment in Tier I securities issued or guaranteed by EU or OECD governments, agencies or instrumentality's, commercial banks and corporations.

The most commonly used are listed below:

Government backed securities: debt instruments issued by Governments

Corporate paper: short term obligations with maturities ranging from overnight to 180 days issued by banks, corporations and other borrowers.

Certificates of deposit: debt instruments issued by banks that pay interest – periodically or at maturity – and principal at maturity.

Time deposits: A deposit in an interest paying account that requires the money to remain on account for a specific length of time.

2. Risk management

What investment restrictions are placed on the Funds?
A soft limit of no more than 10% in any single security, although there are circumstances in which higher holdings are permitted.

Each sub fund typically has at least 50 separate investments.

Are the sub funds separated?
Yes, each sub fund has a separate portfolio of assets. In other words the Fund's custodian cash in the three major currencies is spread across five separate sub funds, each typically with at least 50 underlying investments.

In the worst case scenario, what is the maximum loss the Pension Fund could incur?
In the event that one of the underlying investments in one of the sub funds failed, then the maximum loss suffered by the Essex Pension Fund would be its proportionate share of that underlying investment.

Does that value of the GLF form part of the balance sheet of BNP Paribas (the bank) or Northern Trust (the bank)?
No. The pension funds cash placed in the GLF will be reflected in the balance sheet of the sub fund.

How are the Essex Fund's mandates distributed between the two GLFs as at 1 March 2018?

	BNP Paribas GLF	**Northern Trust GLF**
	£m	**£m**
Aviva	33.2	-
Baillie Gifford	-	11.7
Stewart Investors	-	24.4
Hamilton Lane	24.5	-
Marathon	-	11.2
Longview	-	2.6
Cash Account	-	15.7
Total	**57.7**	**65.6**

Is there a maximum amount allowed in one GLF?
Yes. The Pension Fund Treasury Management Strategy states:

- Northern GLF - £80m (no change on an operational basis)
  Northern GLF - £150m (on a temporary basis to facilitate the redeployment of assets)

- BNP Paribas GLF - £60m (no change on an operational basis)
- BNP Paribas GLF - £150m (on a temporary basis to facilitate the redeployment of assets)

What notice period is required to withdraw funds?
Each Fund has a daily cut off time for dealing. To withdraw Funds on the same day would require notice prior to the cut off deadline.

3. Interest

What interest rate is payable?
Net annualised interest rates (i.e. net of fees) based on year ended 31 January 2018 on the four sub funds used are set out in the table below. If the GLFs were not used, the cash balance (referred to as "idle cash") would attract interest from the Custodian.

	BNP Paribas GLF	Northern Trust GLF
Sterling	0.1%	0.1%
US Dollar	1.2%	1.0%

4. Ratings

How are the GLFs rated?
In summary all are AAA rated.

BNP Paribas
The Funds have obtained and will seek to maintain the following:

AAA by Standard and Poor's
AAA/mmf by Fitch ratings
Aaa-mf by Moody's.

Northern Trust
The Funds have obtained and will seek to maintain the following:

AAAf S1+ by Standard and Poor's
Aaa-mf by Moody's

What is the definition of the ratings?

Standard & Poor's AAA rating*: "An obligation rated 'AAA' has the highest rating assigned by Standard & Poor. The obligor's capacity to meet its financial commitment on the obligation is extremely strong".*
*Standard & Poor's Short Term rating (A-1): "*An obligor rated 'A-1' has strong capacity to meet its financial commitments. It is rated in the highest category by Standard & Poor's. Within this category, certain obligors are designated with a plus sign (+). This indicates that the obligor's capacity to meet its financial commitments is extremely strong".
Moody's Aaa-mf rating: *"Money market funds rated Aaa-mf have very strong ability to meet the dual objectives of providing liquidity and preserving capital".*
Fitch AAA/mmf rating: *"Denote extremely strong capacity to achieve money market fund's investment objective of preserving principal and providing shareholder liquidity through limiting credit, market, and liquidity risk. This capacity is strongly protected from foreseeable events".*

Investment Team
March 2018

Annex 3.1

NORTHERN TRUST GLOBAL FUNDS PLC

INVESTMENT RESTRICTIONS

The investment restrictions applying to each Fund of the Company under the Regulations are set out below. These are, however, subject to the qualifications and exemptions contained in the Regulations and in the Central Rules. Any additional investment restrictions for other Funds will be formulated by the Directors at the time of the creation of such Fund with the prior approval of the Central Bank and detailed in the relevant Supplement.

Where a Fund inadvertently breaches the limitations set out below, due to unforeseen events arising following the purchase of the securities, the Investment Adviser will sell such securities as soon as practicable taking into account the best interests of the Shareholders.

The Directors may from time to time impose such further investment restrictions as shall be compatible with or in the interest of the Shareholders.

1. Permitted Investments

Investments of a Fund are confined to:

1.1. Transferable securities and Money Market Instruments which are either admitted to official listing on a stock exchange in an EU Member State or non-EU Member State or which are dealt on a market which is regulated, operates regularly, is recognised and open to the public in an EU Member State or non-EU Member State;

1.2. Recently issued transferable securities which will be admitted to official listing on a stock exchange or other market (as described above) within a year;

1.3. Money Market Instruments other than those dealt on a regulated market;

1.4. Units of UCITS;

1.5. Units of AIFs;

1.6. Deposits with credit institutions; and

1.7. FDIs.

2. Investment Restrictions

2.1. A Fund may invest no more than 10% of net assets in transferable securities and Money Market Instruments other than those referred to in paragraph 1.

2.2. A Fund may invest no more than 10% of net assets in recently issued transferable securities which will be admitted to official listing on a stock exchange or other market (as described in paragraph 1.1) within a year. This restriction will not apply in relation to investment by the Fund in certain US securities known as Rule 144A securities provided that:

2.2.1. the securities are issued with an undertaking to register with the US Securities and Exchanges Commission within one year of issue; and

2.2.2. the securities are not illiquid securities i.e. they may be realised by the Fund within seven days at the price, or approximately at the price, at which they are valued by the Fund.

2.3. A Fund may invest no more than 10% of net assets in transferable securities or Money Market Instruments issued by the same body provided that the total value of transferable securities and Money Market Instruments held in the issuing bodies in each of which it invests more than 5% is less than 40%.

2.4. The limit of 10% (in 2.3) is raised to 25% in the case of bonds that are issued by a credit institution which has its registered office in an EU Member State and is subject by law to special public supervision designed to protect bond-holders. If a Fund invests more than 5% of its net assets in these bonds issued by one issuer, the total value of these investments may not exceed 80% of the Net Asset Value of the Fund.

2.5. The limit of 10% (in 2.3) is raised to 35% if the transferable securities or Money Market Instruments are issued or guaranteed by an EU Member State or its local authorities or by a non-EU Member State or public international body of which one or more EU Member States are members.

2.6. The transferable securities and Money Market Instruments referred to in 2.4. and 2.5 shall not be taken into account for the purpose of applying the limit of 40% referred to in 2.3.

2.7. A Fund may not invest more than 20% of net assets in deposits made with the same credit institution.

Deposits with any one credit institution, other than credit institutions authorised in the EEA or credit institutions authorised within a signatory state (other than an EEA Member State) to the Basle Capital Convergence Agreement of July 1988 (Switzerland, Canada, Japan, US) or credit institutions located in Jersey, Guernsey, the Isle of Man, Australia or New Zealand held as ancillary liquidity, must not exceed 10% of net assets.

This limit may be raised to 20% in the case of deposits made with the Depositary.

2.8. The risk exposure of a Fund to a counterparty to an OTC derivative may not exceed 5% of net assets.

This limit is raised to 10% in the case of credit institutions authorised in the EEA; credit institutions authorised within a signatory state (other than an EEA member state) to the Basle Capital Convergence Agreement of July, 1988 or a credit institution authorised in Jersey, Guernsey, the Isle of Man, Australia or New Zealand.

2.9. Notwithstanding paragraphs 2.3, 2.7 and 2.8 above, a combination of two or more of the following issued by, or made or undertaken with, the same body may not exceed 20% of net assets:

2.9.1. investments in transferable securities or Money Market Instruments;

2.9.2. deposits; and/or

2.9.3. counterparty risk exposures arising from OTC derivatives transactions.

2.10. The limits referred to in 2.3, 2.4, 2.5, 2.7, 2.8 and 2.9 above may not be combined, so that exposure to a single body shall not exceed 35% of net assets.

2.11. Group companies are regarded as a single issuer for the purposes of 2.3, 2.4, 2.5, 2.7, 2.8 and 2.9. However, a limit of 20% of net assets may be applied to investment in transferable securities and Money Market Instruments within the same group.

2.12. A Fund may invest up to 100% of net assets in different transferable securities and Money Market Instruments issued or guaranteed by any EU Member State, its local authorities, non-EU Member States or public international bodies of which one or more EU Member States are members or any of the following:

OECD Member States
Government of Brazil (provided the relevant issues are investment grade)
Government of India (provided the relevant issues are investment grade)
Government of Singapore
European Investment Bank
European Bank for Reconstruction & Development
International Finance Corporation
International Monetary Fund
Euratom
The Asian Development Bank, Council of Europe
Eurofima
African Development Bank
The World Bank
The International Bank for Reconstruction & Development
The Inter American Development Bank
European Union, European Central Bank
Federal National Mortgage Association ("Fannie Mae")
Federal Home Loan Mortgage Corporation ("Freddie Mac")
Government National Mortgage Association ("Ginnie Mae")

Student Loan Marketing Association ("Sallie Mae")
Federal Home Loan Bank
Federal Farm Credit Bank
Tennessee Valley Authority and Straight-A Funding LLC

The Fund must hold securities from at least 6 different issues, with securities from any one issue not exceeding 30% of net assets.

3. Investment in Collective Investment Schemes (“CIS")

3.1. A Fund may not invest more than 10% of net assets in any one CIS.

3.2. Investment in AIFs may not, in aggregate, exceed 30% of net assets.

3.3. Any CIS in which a Fund invests must be prohibited from investing more than 10% of net assets in other open-ended CIS.

3.4. When a Fund invests in the units of other CIS that are managed, directly or by delegation, by the Fund’s management company or by any other company with which the Fund’s management company is linked by common management or control, or by a substantial direct or indirect holding, that management company or other company may not charge subscription, conversion or redemption fees on account of the Fund’s investment in the units of such other CIS.

3.5.Where a commission (including a rebated commission) is received by the Fund’s investment adviser by virtue of an investment in the units of another CIS, this commission must be paid into the property of the Fund.

4. Index Tracking UCITS

4.1. A Fund may invest up to 20% of net assets in shares and/or debt securities issued by the same body where the investment policy of the Fund is to replicate an index which satisfies the criteria set out in the Central Bank Rules and is recognised by the Central Bank.

4.2. The limit in 4.1 may be raised to 35%, and applied to a single issuer, where this is justified by exceptional market conditions.

5. General Provisions

5.1. An investment company, or management company acting in connection with all of the CIS it manages, may not acquire any shares carrying voting rights which would enable it to exercise significant influence over the management of an issuing body.

5.2. A Fund may acquire no more than:

5.2.1. 10% of the non-voting shares of any single issuing body;

5.2.2. 10% of the debt securities of any single issuing body;

5.2.3. 25% of the units of any single CIS;

5.2.4. 10% of the Money Market Instruments of any single issuing body.

The limits laid down in 5.2.2, 5.2.3 and 5.2.4 above may be disregarded at the time of acquisition if at that time the gross amount of the debt securities or of the Money Market Instruments, or the net amount of the securities in issue cannot be calculated.

5.3. 5.1 and 5.2 shall not be applicable to:

5.3.1. transferable securities and Money Market Instruments issued or guaranteed by an EU Member State or its local authorities;

5.3.2. transferable securities and Money Market Instruments issued or guaranteed by a non-EU Member State;

5.3.3. transferable securities and Money Market Instruments issued by public international bodies of which one or more EU Member States are members;

5.3.4. shares held by a Fund in the capital of a company incorporated in a non-EU Member State which invests its assets mainly in the securities of issuing bodies having their registered offices in that state, where under the legislation of that state such a holding represents the only way in which the Fund can invest in the securities of issuing bodies of that state. This waiver is applicable only if in its investment policies the company from the non-EU Member State complies with the limits laid down in 2.3 to 2.11, 3.1, 3.2, 5.1, 5.2, 5.4, 5.5 and 5.6 and provided that where these limits are exceeded, paragraphs 5.5 and 5.6 below are observed;

5.3.5. shares held by an investment company in the capital of subsidiary companies carrying on only the business of management, advice or marketing in the country where the subsidiary is located, in regard to the repurchase of shares at Shareholders' request exclusively on their behalf.

5.4. The Company need not comply with the investment restrictions herein when exercising subscription rights attaching to transferable securities or Money Market Instruments which form part of their assets.

5.5. The Central Bank may allow recently authorised Funds to derogate from the provisions of 2.3 to 2.12, 3.1, 3.2 4.1 and 4.2 for six months following the date of their authorisation, provided they observe the principle of risk spreading.

5.6. If the limits laid down herein are exceeded for reasons beyond the control of the Company, or as a result of the exercise of subscription rights, the Company must adopt as a priority objective for its sales transactions the remedying of that situation, taking due account of the interests of its Shareholders.

5.7. Neither the Company nor a Fund, may carry out uncovered sales of:

5.7.1. transferable securities;

5.7.2. Money Market Instruments;

5.7.3. units of CIS; or

5.7.4. FDIs.

5.8. A Fund may hold ancillary liquid assets.

6. FDIs

6.1. The Fund's global exposure relating to FDI must not exceed its total Net Asset Value (this provision may not be applicable to Funds that calculate their global exposure using the VaR methodology as disclosed in the relevant Supplement).

6.2. Position exposure to the underlying assets of FDIs, including embedded FDIs in transferable securities or Money Market Instruments, when combined where relevant with positions resulting from direct investments, may not exceed the investment limits set out in the Central Bank Rules. (This provision does not apply in the case of index based FDIs provided the underlying index is one which meets with the criteria set out in the Central Bank Rules.)

6.3. A Fund may invest in FDIs dealt in OTC derivatives provided that the counterparties to OTC transactions are institutions subject to prudential supervision and belonging to categories approved by the Central Bank.

6.4. Investment in FDIs is subject to the conditions and limits laid down by the Central Bank

BNP PARIBAS INSTICASH – GLOBAL LIQUIDITY FUND

INVESTMENT RESTRICTIONS
For the purpose of this Appendix 1, the following definitions apply:

“Member State”: Means member state of the European Union. The states that are contracting parties to the Agreement creating the European Economic Area other than the Member States of the European Union, within the limits set forth by this Agreement and related acts are considered as equivalent to Member States of the European Union.
“Third Country”: Means a country other than a Member State.

1. A sub-fund’s investments shall comprise only one or more of the following:

a) transferable securities and money market instruments admitted to or dealt in on a regulated market as defined by Directive 2004/39;

b) transferable securities and money market instruments dealt in on another regulated market in a Member State, which operates regularly and is recognised and open to the public;

c) transferable securities and money market instruments admitted to official listing on a stock exchange in a country which is not a European Union Member State or dealt in on another regulated market in a country which is not a European Union Member State which operates regularly and is recognised and open to the public;

d) recently issued transferable securities and money market instruments, provided that:

(i) the terms of issue include an undertaking that an application will be made for admission to official listing on a stock exchange or to another regulated market which operates regularly and is recognised and open to the public; and

(ii) the admission is secured within one year of the issue;

e) units or shares in UCITS authorised according to Directive 2009/65 and/or other UCIs within the meaning of Article 1(2)(a) and (b) of the Directive 2009/65, whether or not established in a Member State, provided that:

(i) such other UCIs are authorised under laws which provide that they are subject to supervision considered by the CSSF to be equivalent to that laid down in EU legislation, and that cooperation between authorities is sufficiently ensured;

(ii) the level of protection to unitholders or shareholders in these other UCIs is equivalent to that provided for unitholders or shareholders in a UCITS, and in particular that the rules on assets segregation, borrowings, lending, and uncovered sales of transferable securities and money market instruments are equivalent to the requirements of Directive 2009/65;

(iii) the business of these other UCIs is reported in semi-annual interim and annual reports to enable an assessment to be made of the assets and liabilities, income and operations over the reporting period; and

(iv) no more than 10% of the assets of the UCITS or of the other UCIs whose acquisition is contemplated, can, according to their management regulations or articles of association, be invested in aggregate in units or shares of other UCITS or other UCIs;

f) deposits with credit institution which are repayable on demand or have the right to be withdrawn and maturing in no more than 12 months, provided that the credit institution has its registered office in a Member State or, if the credit institution has its registered office in a Third Country, provided that it is subject to prudential rules considered by the CSSF as equivalent to those laid down in EU legislation;

g) financial derivative instruments, including equivalent cash-settled instruments, dealt in on a regulated market referred to in points a), b) and c) above or financial derivative instruments dealt in over-the-counter (OTC) derivatives, provided that:

(i) the underlying of the derivative consists of instruments covered by this paragraph1., financial indices, interest rates, foreign exchange rates or currencies, in which the corresponding sub-fund may invest according to its investment objectives as stated in the Company's Articles of Association.

(ii) the counterparties to OTC derivatives transactions are institutions subject to prudential supervision and belonging to the categories approved by the CSSF, and

(iii) the OTC derivatives are subject to reliable and verifiable valuation on a daily basis and can be sold, liquidated or closed by an offsetting transaction at any time and at their fair value at the Company's initiative;

h) money market instruments other than those dealt in on a regulated market, which fall under Article 1 of the Law, if the issue or issuer of such instruments is itself regulated for the purpose of protecting investors and savings, provided that they are:

(i) issued or guaranteed by a central, regional or local authority, by a central bank of a Member State, the European Central Bank, the European Union or the European Investment Bank, a Third Country or, in the case of a Federal State, by one of the members making up the federation or, by a public international body to which one or more European Union Member States belong;

(ii) issued by a company any securities of which are dealt in on regulated markets referred to in Section 1. paragraph a), b) or c) above;

(iii) issued or guaranteed by an establishment subject to prudential supervision, in accordance with criteria defined by EU law, or by an establishment which is subject to and complies with prudential rules considered by the CSSF to be at least as stringent as those laid down by EU legislation; or

(iv) issued by other bodies belonging to the categories approved by the CSSF provided that the investments in such instruments are subject to investor protection equivalent to that laid down in points (i), (ii) or (iii)first, second or third sub-clauses immediately preceding, and provided that the issuer is a company whose capital and reserves amount to at least EUR 10 000 000 and which presents and publishes its annual accounts in accordance with the Directive 78/660, is an entity which, within a group of companies which includes one or several listed companies, is dedicated to the financing of the group or is an entity which is dedicated to the financing of securitisation vehicles which benefit from a banking liquidity line.

2. A sub-fund shall not, however:

a) invest more than 10% of its assets in transferable securities, or money market instruments other than those referred to in Section 1.; or

b) acquire either precious metal or certificates representing them.

A sub-fund may hold ancillary liquid assets.

3. The Company may acquire movables and immovable property indispensable for the direct performance of its activity.

4.
a) A sub-fund shall not invest no more than:

(i) 10% of its assets in transferable securities or money market instruments issued by the same body; or
(ii) 20% of its assets in deposits made with the same body.

The risk exposure to a counterparty of a sub-fund in an OTC derivative transaction shall not exceed either:

(i) 10% of its assets when the counterparty is a credit institution referred to Section 1. paragraph f); or

(ii) 5% of its assets, in other cases.

b) The total value of the transferable securities and the money market instruments held by a sub-fund in the issuing bodies in each of which it invests more than 5% of its assets shall not exceed 40% of the value of its assets. That limitation shall not apply to deposits or OTC derivative transactions made with financial institutions subject prudential supervision. Notwithstanding the individual limits laid down in paragraph a), a sub-fund shall not combine, where this would lead to investment of more than 20% of its assets in a single body, any of the following:

(i) investments in transferable securities or money market instruments issued by that body;

(ii) deposits made with that body; or

(iii) exposure arising from OTC derivatives transactions undertaken with that body.

c) The 10% limit laid down in the paragraph a) point (i) may be raised to a maximum of 35% if the transferable securities or money market instruments are issued or guaranteed by a Member State, by its local authorities, by a Third Country or by public international body to which one or more Member States belong.

d) The 10% limit laid down in the paragraph a) point (i) may be raised to a maximum of 25% where bonds are issued by a credit institution which has its registered office in a Member State and is subject by law to special supervision designed to protect bond-holders. In particular, sums deriving from the issue of those bonds shall be invested in accordance with the law in assets which, during the whole period of validity of the bonds, are capable of covering claims attaching to the bonds and which, in the event of failure of the issuer, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest.

Where a sub-fund invests more than 5% of its assets in the bonds referred to in paragraph a) which are issued by a single issuer, the total value of these investments shall not exceed 80% of the value of the assets of the sub-fund.

e) The transferable securities and money market instruments referred to in paragraphs c) and d) shall not be taken into account for the purpose of applying the limit of 40% referred to in paragraph b).

The limits provided in paragraph a), b), c) and d) shall not be combined, and thus investments in transferable securities or money market instruments issued by the same body or in deposits or derivative instruments made with this body carried out in accordance with paragraph a), b), c) and d) shall not exceed in total 35% of the assets of the sub-fund. Companies which are grouped together into a consolidated accounting entity as defined by Directive 83/349 or in accordance with recognised international accounting rules are considered as a single entity for the calculation of the limits stipulated in this Section 4.

A single sub-fund may invest a cumulative total of up to 20% of its assets in the transferable securities and money market instruments of a single group.

5. Without prejudice to the limits laid down in Section 8., the limits laid down in Section 4. are raised to a maximum of 20% for investments in shares or debt securities issued by the same body, when the aim of the sub-fund's investment policy is to replicate the composition of a certain stock or debt securities index which is recognised by the CSSF, on the following basis:

(i) its composition is sufficiently diversified;

(ii) the index represents an adequate benchmark for the market to which it refers; and

(iii) it is published in an appropriate manner.

This limit of 20% shall be raised to a maximum 35% where that proves to be justified by exceptional market conditions(such as, but not limited to, disruptive market conditions or extremely volatile markets) in particular in regulated markets where certain transferable securities or money market instruments are highly dominant. The investment up to that limit shall be permitted only for a single issuer.

6. As an exception to Section 4., in accordance with the principle of risk-spreading, a sub-fund shall invest up to 100% of its assets in different transferable securities and money market instruments issued or guaranteed by a Member State, one or more of its local authorities, a Third Country part of the OECD, Brazil, Russia, Singapore and South Africa, or a public international body to which one or more Member States belong.
Such a sub-fund shall hold securities from at least six different issues, but securities from any single issue shall not account for more than 30% of its total assets.

7.
a) A sub-fund may acquire the units or shares in UCITS or other UCIs referred to in Section 1. paragraph e), provided that no more than 20% of its assets are invested in units or shares of a single UCITS or other UCI. For the purposes of the application of this investment limit, each sub-fund in a multi-sub-fund UCI, as defined by Article 181 of the Law, is considered as a separate issuer, provided that the principle of segregation of the commitments of the different sub-funds with regard to third parties is assured.

b) Investments made in units or shares of UCIs other than UCITS shall not exceed, in aggregate, 30% of the assets of a sub-fund. Where a sub-fund has acquired units or shares of another UCITS or UCIs, the assets of the respective UCITS or other UCIs are not combined for the purposes of the limits laid down in Section 4.

c) Due to the fact that the Company may invest in UCI units, or shares, the investor is exposed to a risk of fees doubling (for example, the management fees of the UCI in which the Company is invested).

A sub-fund may not invest in a UCITS, or other UCI (underlying), with a management fee exceeding 3% per annum.

Where a sub-fund invests in the units or shares of other UCITS or UCIs that are managed, directly or by delegation, by the same management company or by any other company with which the management company is linked by common management or control, or by a substantial direct or indirect holding, the sub-fund will not incur any entry or exit costs for the units or shares of these underlying assets.

The maximum annual management fee payable directly by the sub-fund is defined in Book II.

8.
a) The Company shall not acquire any shares carrying voting rights which would enable it to exercise significant influence over the management of an issuing body.

b) A sub-fund may acquire no more than:

(i) 10% of the non- voting shares of a single issuing body;

(ii) 10% of debt securities of a single issuing body;

(iii) 25% of units or shares of a single sub-fund of UCITS or other UCI within the meaning of Article 2 Paragraph 2 of the Law; or

(iv) 10% of the money market instruments of a single issuing body.

The limits laid down in points (ii), (iii) and (iv) may be disregarded at the time of acquisition if, at that time, the gross amount of debt securities or of the money market instruments, or the net amount of the securities issued, cannot be calculated.

c) Paragraph a) and b) above do not apply with regard to:

(i) transferable securities and money market instruments issued or guaranteed by a Member State or its local authorities;

(ii) transferable securities and money market instruments issued or guaranteed by a country which is not a European Union Member State;

(iii) transferable securities and money market instruments issued by a public international body to which one or more European Union Member State belong;

(iv) shares held by the Company in the capital of a company incorporated in a Third Country not member of the European Union investing its assets mainly in securities of issuing bodies having their registered offices in that country, where under the legislation of that country, such a holding represents the only way in which the Company can invest in the securities of issuing of that country. This derogation shall apply only if in its investment policy the company from the Third Country not member of the European Union complies with the limits laid down in Sections 3, 6 and 7 paragraph a) and b). Where the limits set in Sections 4. and 7. are exceeded, Section 9. shall apply *mutatis mutandis*;

9. The sub-funds are not required to comply with the limits laid down in this Appendix when exercising subscription rights attaching to transferable securities or money market instruments which form part of their assets.

While ensuring observance of the principle of risks spreading, recently authorised sub-funds are allowed to derogate from Section 4, 5, 6 and 7 for six months following the date of their authorisation.

If these limits are exceeded for reasons beyond the control of the sub-fund or as a result of the exercise of subscription rights, the sub-fund shall adopt as a priority objective for its sales transactions the remedying of that situation, taking due account of the interests of its shareholders.

10. A sub-fund can acquire currencies through back-to-back loans.
A sub-fund may borrow the following, provided that these loans:

a) are temporary and represent a maximum of 10% of its assets;

b) allow the acquisition of immovable property indispensable to the direct exercise of its activities and represent a maximum of 10% of its assets.

If a sub-fund is authorised to borrow under points a) and b), these loans must not exceed 15% of its total assets.

11. Without prejudice to the application of Sections 1., 2. and Appendix 2, a sub-fund shall not grant loans or act as a guarantor on behalf of third parties.
This shall not prevent a sub-fund from acquiring transferable securities, money market instruments or other financial instruments referred to in Section 1. paragraph e), g) and h), which are not fully paid.

12. A sub-fund shall not carry out uncovered sales of transferable securities, money market instruments or other financial instruments referred to in Section 1. paragraph e), g) and h).

13. By way of derogation of the above restriction, a sub-fund designed as “the Feeder” may invest:

a) at least 85% of its assets in units, or shares of another UCITS or another sub-fund of UCITS (the “Master”);

b) up to 15% of its assets in one or more of the following:

- ancillary liquid assets,
- financial derivative instruments, which may be used only for hedging purpose, in accordance with Section 1. paragraph g) and Appendix 2;
- movable and immovable property which is essential for the direct pursuit of its business.

14. A sub-fund may acquire shares of one or more other sub-funds of the Company (the target sub-fund), provided that:

- the target sub-fund does not, in turn, invest in the sub-fund;
- the proportion of assets that each target sub-fund invests in other target sub-funds of the Company does not exceed 10%;
- any voting rights attached to the shares of the target sub-funds are suspended for as long as they are held by the sub-fund and without prejudice to the appropriate treatment in the accounts and the periodic reports; and
- in any event, for as long as these target sub-fund shares are held by the Company, their value shall not be taken into consideration for the calculation of the net assets of the Company for the purposes of verifying the minimum threshold of net assets required by the law.

As a general rule, the Board of Directors reserves the right to introduce other investment restrictions at any time when indispensable for conforming to the laws and regulations in force in certain states where the Company’s shares may be offered and sold. On the other hand, where permitted by current regulations applicable to the Company, the Board of Directors reserves the right to exempt one or more sub-funds from one or more of the investment restrictions specified above. These exceptions will be mentioned in the investment policies summarised in Book II for each of the sub-funds concerned.

Essex Pension Fund Investment Steering Committee	AGENDA ITEM 5
date: 28 March 2018	

Market Background and Outlook Q4 2017
Report by Hymans Robertson

Enquiries to Kevin McDonald on 0333 0138 488

1. Purpose of Report

1.1 To update the ISC on recent market conditions.

2. Recommendation

2.1 That the Committee should note the content of the report.

Capital Markets Outlook Q4 2017

Essex Pension Fund

March 2018

Matt Woodman. Senior Investment Consultant
Rebecca Craddock-Tailor, Associate Investment Consultant

For and on behalf of Hymans Robertson LLP

Initial Comments on post year end volatility

After a relatively benign 2017 with asset markets continuing their strength, the end of January/beginning of February 2018 has seen both an increase in volatility and some high profile corporate issues with both Carillion and Capita facing challenges.

At the time of writing (7 February) equity markets (as measured by the FTSE 100) had fallen some 8% since the market highs reached in mid-January. Although significant in terms of short term volatility, this should be considered in the context of the multi-year strength of equity markets. Further, we view this as a reality check that equity markets are risky, experience volatility and must be considered in a long term perspective. It also strengthens our resolve around implementing de-risking at opportune times (as the ISC are discussing).

The abrupt turn in sentiment suggests some market participants may have forgotten the realities of equity investment, after the incredibly low levels of volatility throughout 2017. The acceleration in the sell-off in US equities also suggests that many investors have sought to lock-in recent profits and sell their holdings in case markets fall further, exacerbating the sell-off.

In the absence of any specific triggers, many commentators have been searching for data points, such as strong US wage inflation data, to explain the recent market moves. Although strong US wage inflation data (alongside record low unemployment) would suggest a buoyant backdrop for equity markets, it is the secondary impact on interest rates that have caused concern for investors. US 10-year yields are as high as they have been for four years and haven't sustained significantly higher levels since the middle of 2011. However, while there has clearly been a change to market sentiment, it would be premature to suggest that the fundamental backdrop has changed. The US wage inflation statistic is just one data point and some have highlighted the rise in minimum wage in several US states and an unusual drop in hours worked as potential distorting factors. That said, US monetary policy over the last year has reflected a view in the Federal Reserve that the fall in US inflation was a temporary phenomenon. Last year bond yields tended to rise ahead of monetary policy changes and then drift back lower, as investors were reassured by short-term inflation numbers. The current behaviour of bond yields might be better portrayed as a greater alignment of view between investors and central bankers, rather than a sudden change to the economic outlook. Of course, should inflation expectations start to rise sharply then equity markets (and of course bond markets) would be vulnerable.

Closer to home, UK gilt yields have risen to levels higher than any witnessed in 2017 over short-to-medium durations. However, at longer durations yields are broadly in line with the levels seen at the end of Q3 17.

In summary, the increase in yields and sell-off in equity markets does not appear, at this stage, to reflect any significant change to the fundamental market backdrop. Both movements suggest a short-term market correction, rather than a longer-term market collapse.

In relation to Capita and Carillion, the impact in terms of investment is small (pre the latest news they were less than 0.2% and 0.1% of the FTSE All Share respectively and therefore much less in the global equity approach adopted by Essex). Where we would envisage a greater impact is in relation to admitted bodies in the Fund supported by the covenant of these employers. We would therefore advise consideration of this by the PSB.

Further update to mid-March

Key market indicators:

- There has been upward revision of global growth prospects and employment data has also been robust. Hence, as spare capacity continues to be used up, wage inflation is expected to pick up.

- Given the Fed's dual mandate – inflation target of 2% (as measure by Personal Consumption Expenditures "PCE") and low unemployment target – investors are concerned about Fed's reaction to this backdrop. In other words, the pace and magnitude of base rate hikes and monetary policy tightening is uncertain.

UK company news:

- Investors are becoming increasingly nervous about bonds of high street retailers and food outlets as pressure mounts from online competition and rising input costs. New Look and Prezzo are amongst the high-profile names in "distressed" territory. Both companies are in the process of undergoing "company voluntary arrangement" where lower rents are being negotiated with their respective landlords.

US vs China trade war:

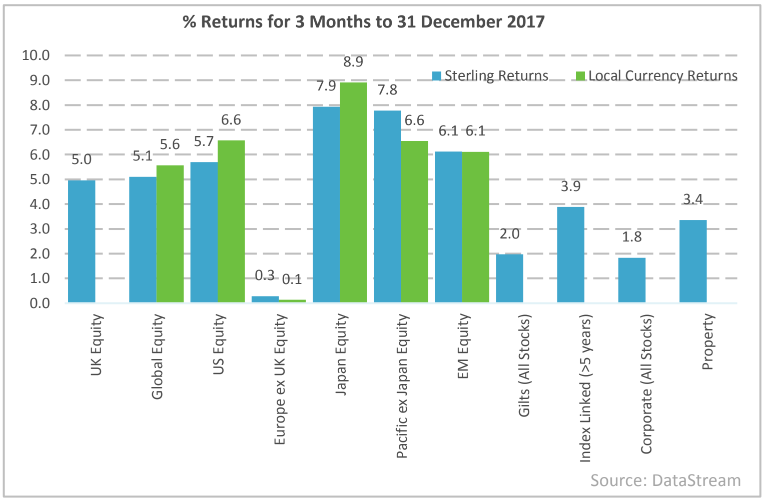
- On the campaign trail, Trump stated he wanted high tariffs on all Chinese goods – 45% in some cases.
- Early signs of this protectionist stance was demonstrated in Trump's administration's recent proposal of a 25% tariff on steel imports and a 10% tariff on aluminium imports from China.
- Despite the headline figures, aluminium and steel exports account for 0.02% of Chinese GDP so will not have a material impact on Chinese economy (Canada is likely to be impacted the most from Trump's new tariffs).
- However, these changes could be the prelude for a 'tit-for-tat trade war' with material losers on both sides.
- Ultimately, higher import costs are likely to lead to lower profits for companies unless they are passed onto the end consumer where they will be subject to higher prices.

Markets

- Since the initial bout of volatility, markets have broadly traded sideways (but with continued volatility). The impact on UK investors in overseas assets has been offset to a degree by sterling weakness.
- Gilt yields are marginally higher than where they started the year.

Market Background for Q4 '17

Economic conditions were supportive of investment markets over the final quarter of 2017: inflation stabilised, corporate earnings continued to rise and indicators suggested that global economic expansion, if anything, was picking up pace. Q3 data confirmed robust growth in the US, Eurozone, and Japan whilst UK growth remained sluggish at 0.4% (albeit still ahead of expectations).

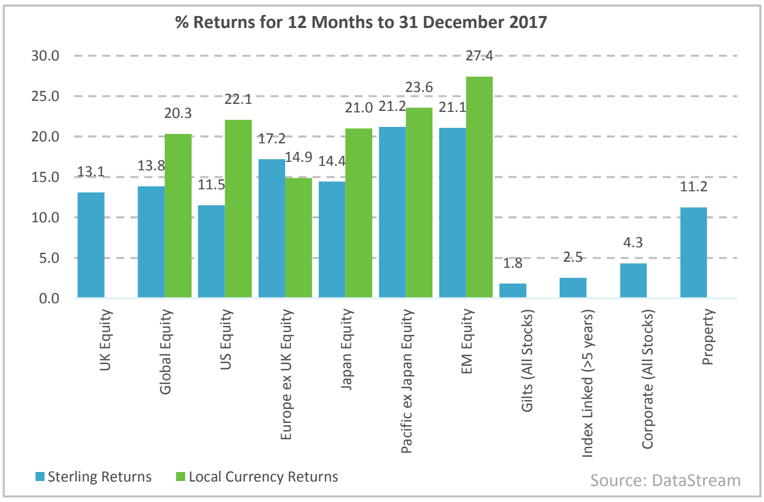


As almost universally expected, the Bank of England's Monetary Policy Committee increased interest rates by 0.25% p.a. to 0.5% p.a. despite sluggish UK economic conditions. There was little surprise about the tightening of monetary policy announced elsewhere – a tapering of quantitative easing in the Eurozone and another US interest rate rise.

Oil prices continued to rise with Brent crude finishing the year at $67 a barrel, the highest price since 2015. Industrial metals were also strong over the quarter – broad price indices for the sector rose over 30% in 2017.

Global equity indices had another strong quarter, bolstered by a continued positive economic outlook. Sentiment was also boosted by the agreement of significant reductions to US corporate tax rates. The best regional equity performance came from Japan which is now enjoying its longest economic expansion since the 1990s. European equities underperformed – economic conditions remain buoyant, but the strength of the euro over the last two years is increasingly seen as likely to depress future profits growth. As might be expected in a market rally, defensive stocks – Healthcare, Telecommunications and Utilities – lagged. The best performers – Basic Materials, Technology and Consumer Services – are typically beneficiaries of economic strength. This has been a familiar trend over 2017 with growth stock significantly outperforming value stocks.

In fixed income, government bonds posted positive returns over the quarter. Long-dated gilt yields (both conventional and index-linked) drifted lower over the quarter, finishing 2017 little changed from the end of 2016.



Credit spreads finished close to end September levels. Some company-specific disappointments from a few major issuers did cause a wobble in the high yield market in particular, but sentiment recovered quickly.

UK commercial property values, as reflected in the IPD UK Monthly Index, have risen further. The very gentle acceleration in the pace of the rise, evident throughout 2017, has persisted. The industrial sector continues to outstrip both office and retail sectors in terms of both total return and rental growth.

Key market data

The tables below provide a summary of key financial indicators over recent periods:

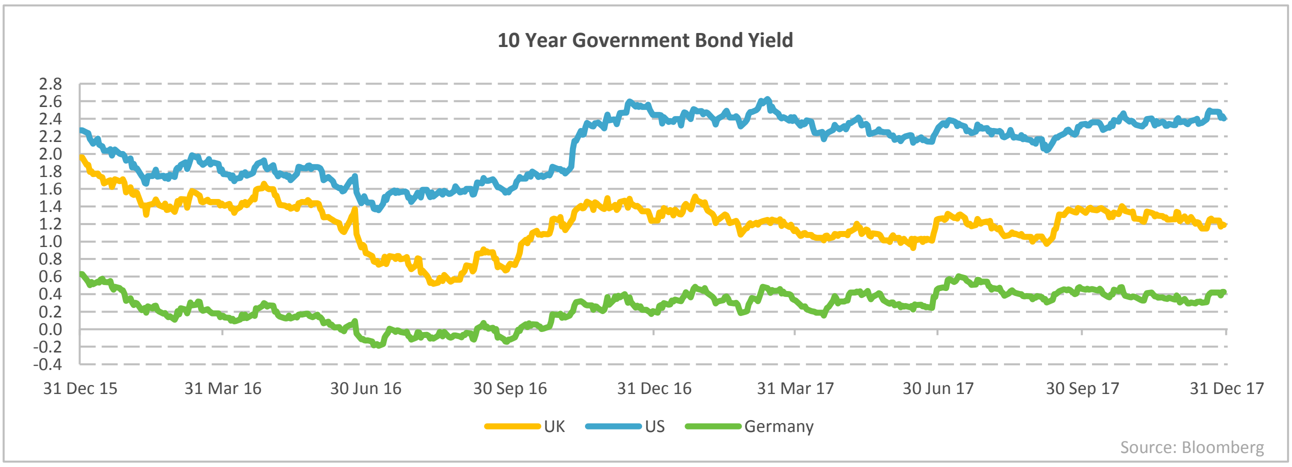
	31.12.16	31.03.17	30.06.17	30.09.17	31.12.17
UK Equity yield	3.5%	3.5%	3.6%	3.7%	3.6%
UK Equity P/E ratio (FTSE)	30.3x	28.3x	27.5x	24.4x	21.2x
Over 15 year gilt yield (p.a.)	1.8%	1.7%	1.8%	1.8%	1.7%
Over 5 year index-linked gilt yield (p.a.)	-1.7%	-1.7%	-1.6%	-1.5%	-1.7%
iBoxx Over 10 year Non-gilt yield (p.a.)	2.9%	2.8%	2.8%	2.9%	2.8%

Source: DataStream

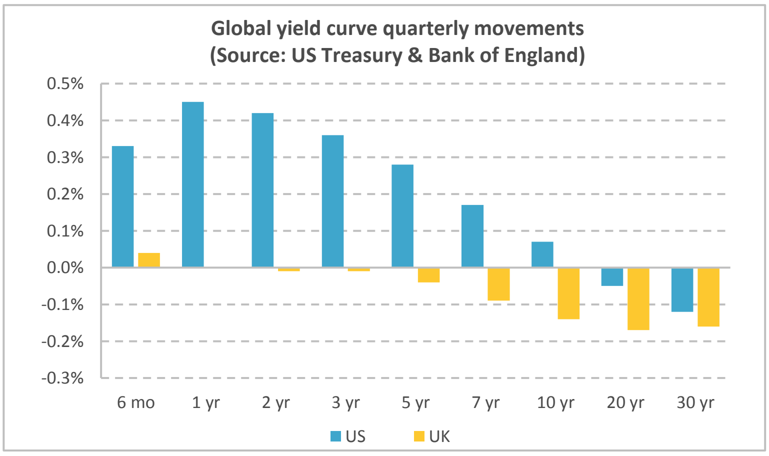
	Year to 31.12.16	Year to 31.12.17	Quarter to 31.03.17	Quarter to 30.06.17	Quarter to 30.09.17	Quarter to 31.12.17
FTSE All Share	16.8%	13.1%	4.0%	1.4%	2.1%	5.0%
Global Equity	29.6%	13.8%	5.8%	0.5%	1.9%	5.1%
Over 15 year gilts	18.5%	3.3%	2.6%	-2.3%	-0.5%	3.7%
Over 5 year index linked gilts	27.4%	2.5%	2.0%	-2.4%	-0.8%	3.9%
All Stocks Non-Gilts	10.6%	4.3%	1.9%	0.5%	0.1%	1.8%
IPD Monthly Index	2.6%	11.2%	2.3%	2.5%	2.7%	3.4%

Source: DataStream

Global Bond Markets



There was a divergence in movements of 10-year sovereign bond yields over the quarter - US yields rose, UK yields fell and European yields moved sideways.

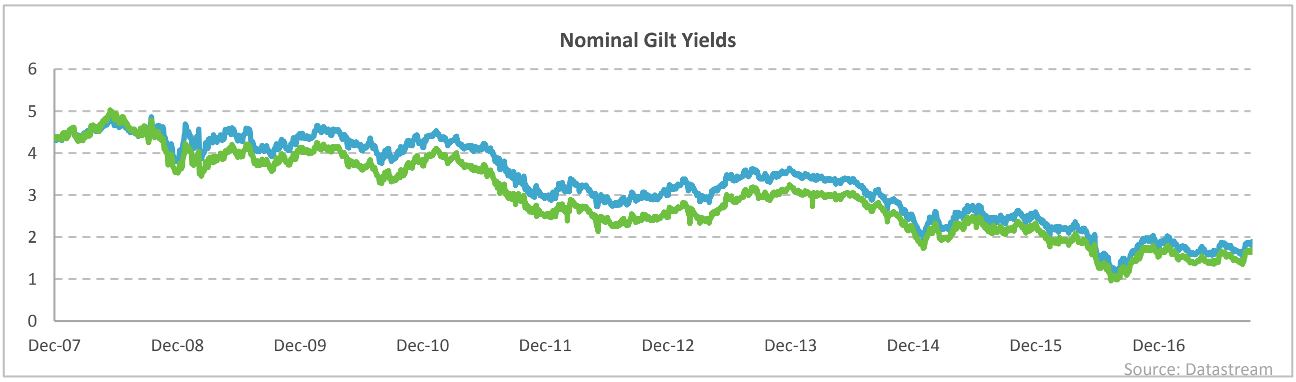


Inflation pressures, outside of the UK, remain subdued, however the expectation is that influences currently acting to depress inflation may not persist. Hence, there was little surprise about the tightening of monetary policy from the major central banks over the quarter.

As expected, the Bank of England's Monetary Policy Committee raised interest rates by 0.25% p.a. to 0.5% p.a. in November 2017. In the US, the Federal Reserve again raised its benchmark interest rate and began its programme of 'quantitative tightening' as economic conditions remained robust. The ECB also announced plans to taper its quantitative easing programme and there was even some speculation that the Bank of Japan may take its foot off the monetary accelerator during 2018.

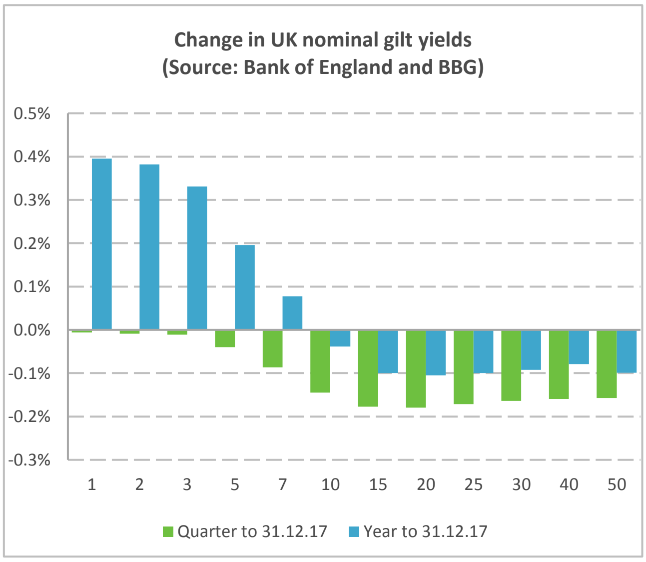
Normalisation of monetary policy is now the default as long as economic conditions remain reasonably robust. One question is where normalisation lands – there are signs that US expectations are to normalise at yields around 3%. Previous expectations suggested normalisation to c4%. That would suggest limited expectation of further increases in long-dated US Government yields.

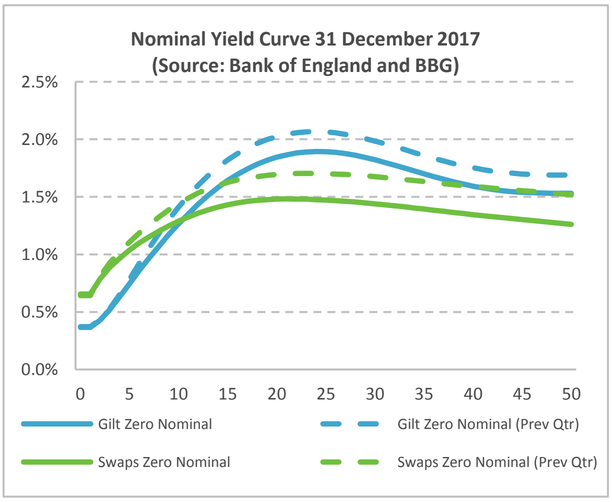
UK Interest Rates

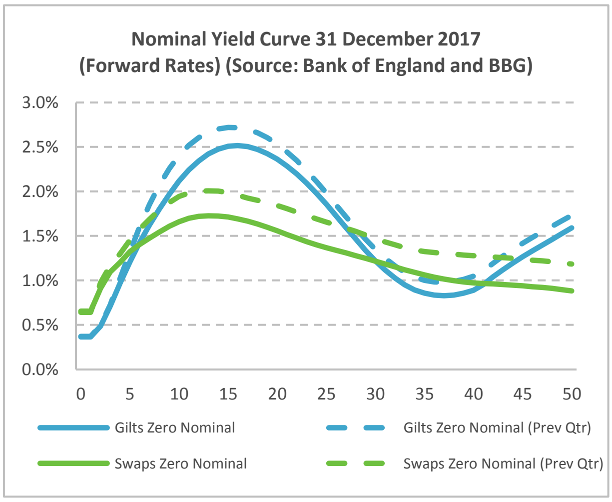


The Bank of England's token increase in UK base rates, from 0.25% to 0.5%, took place in November as expected, justified on the basis that the UK economy was seeing increased inflationary pressures and low unemployment.

Gilts yields have ended 2017 much as they started the year and with probably just as much, if not more, Brexit uncertainty it is unlikely the BoE will raise rates much in coming months. Following the rate rise, Mark Carney struck a dovish tone and suggested only two more rate rises may be needed over the next three years, which caused gilt yields to fall marginally over the quarter as markets priced in rates remaining lower for longer.



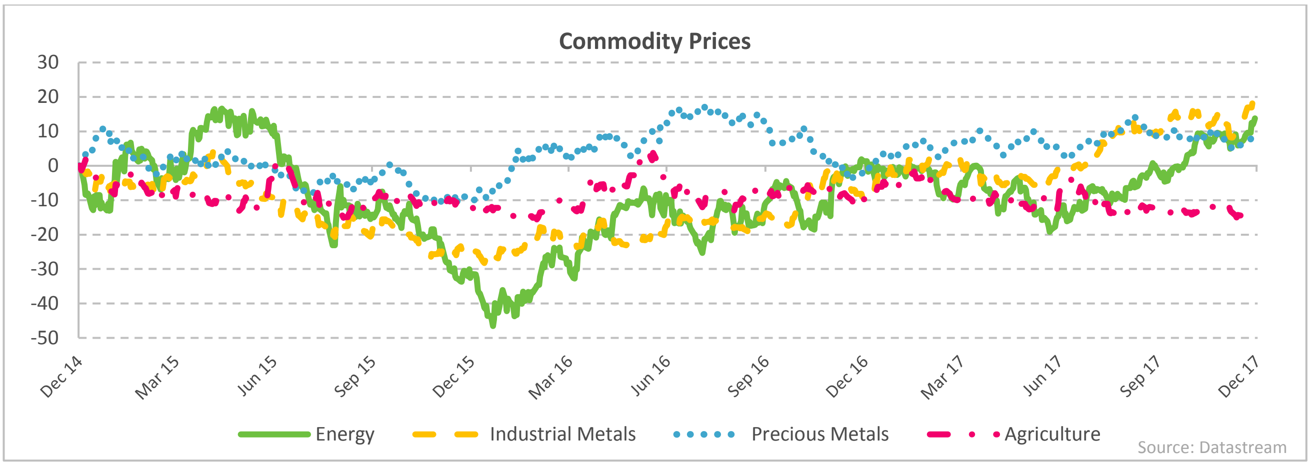




Those concerned with hedging programmes should focus on the anomalies in the yield curve and on the relationship between conventional and index-linked yields as much as the absolute level of yields. Nominal forward gilt yields continue to suggest that there is better value in the medium maturity portion of the gilt curve (10-20 years) than very long maturities (30-50 years).

Inflation and real rates

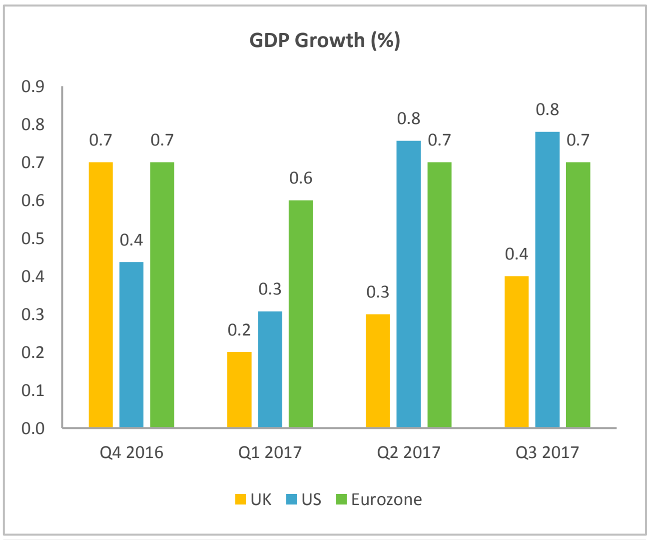
Commodity prices continued to rise over the quarter, underpinned by a rally in energy and industrial metal. Oil prices continued to rise, primarily driven by an agreement among OPEC members, with Brent crude finishing the year at $67 a barrel – the highest price since 2015.

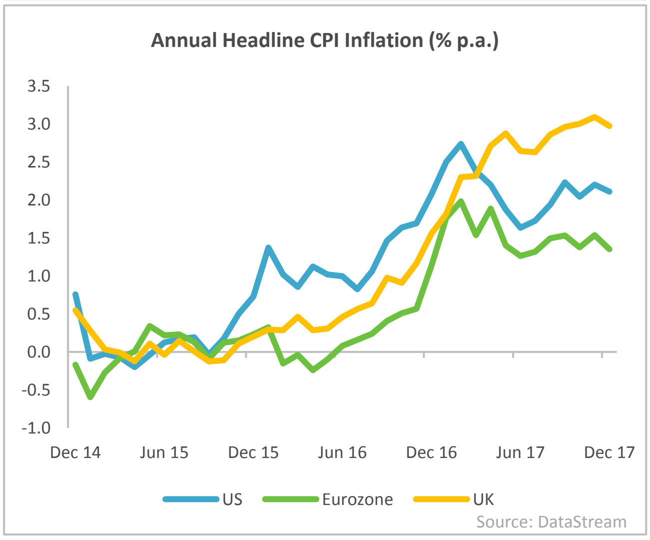


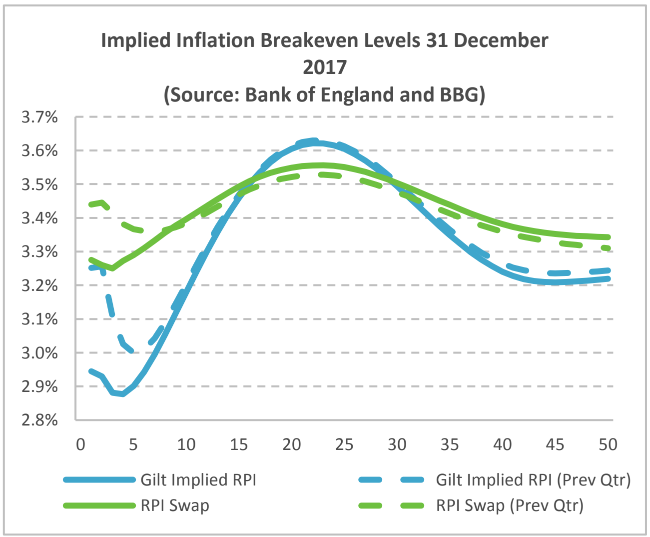
Third quarter GDP figures confirmed robust growth in the US, Eurozone and Japan. The US sustained the 3% annualised growth of the previous quarter, the equivalent number for the Eurozone was 2.5% but that has been sustained for a year now. Japan's seventh successive quarter of growth marked its longest expansion since the 1990s. UK growth was also ahead of expectations, but remains sluggish at 0.4% for Q3. More timely indicators – business surveys, economic surprise indicators – suggest that underlying momentum has remained intact into the new year.

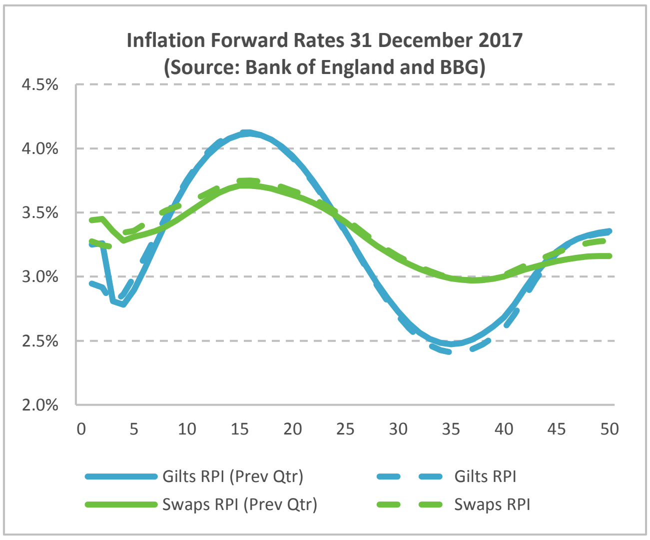
Meanwhile, inflation pressures outside of the UK, remain subdued, particularly where based on core measures (i.e. excluding food and energy). Headline UK CPI inflation rose above 3% for the first time in six years, forcing Mark Carney to write a letter to the Chancellor explaining the overshoot of the BoE's 2% target.

Below-target inflation seems to be a waning concern for central bankers. The potential distorting effects of extreme monetary accommodation on financial markets may be of greater importance as risk premiums remain compressed. In the US and Eurozone at least, there is a view that influences currently acting to depress inflation may not persist.



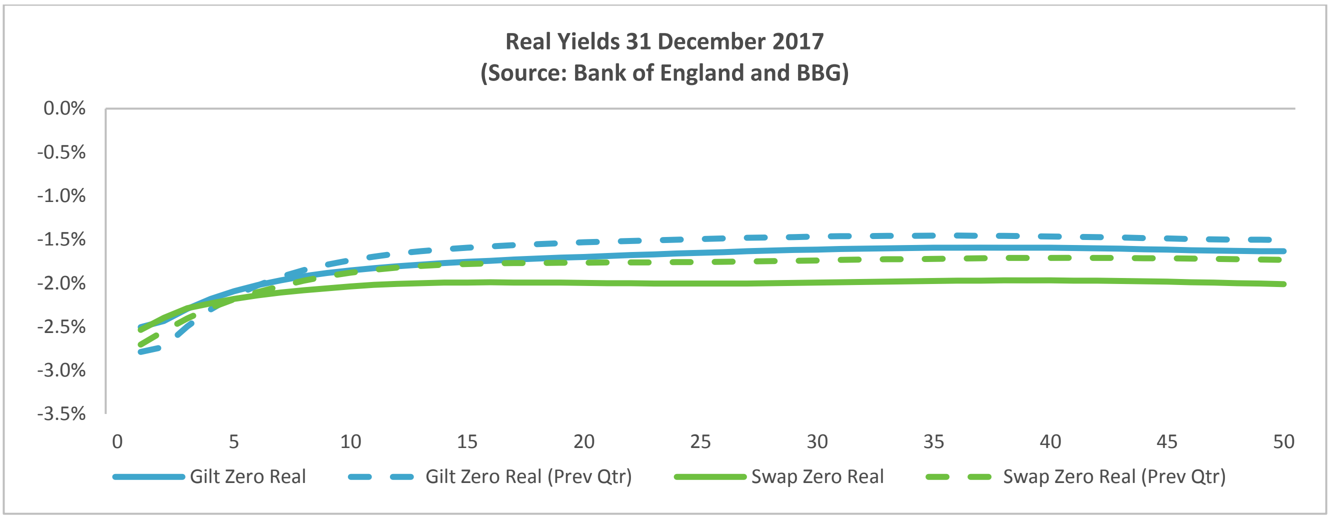






Real yields moved sideways over the quarter and remain very low relative to long-term history. In absolute terms, even allowing for uncertainty about the long-term outlook for the UK economy, real yields on index-linked gilts still reflect hedging demand rather economic fundamentals. Protecting against inflation is expensive, especially in the UK where the demand for index-linked gilts is higher than the supply. Real yields on index-linked gilts (after allowing for RPI assumed to be c.1% p.a. higher than CPI) are yielding less than their German equivalents, and are more than 1% p.a. lower than US Treasury Inflation Protected Securities (TIPS).

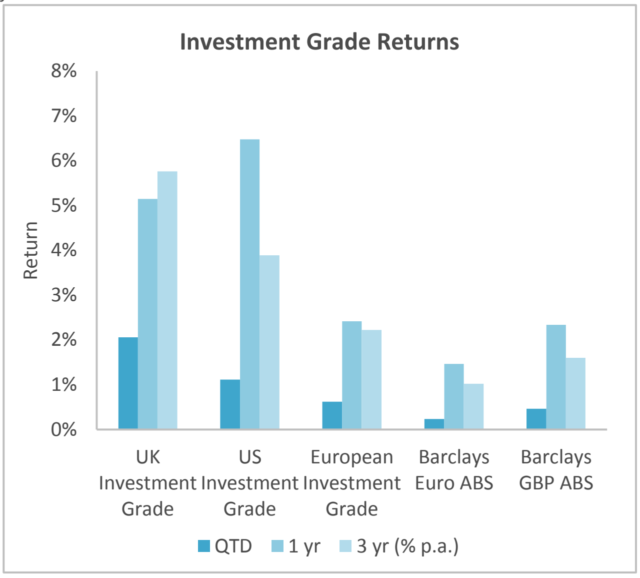
We expect real yields to continue to closely follow nominal yields over 2018, with higher levels of inflation already factored into pricing. An earlier than expected increase in base rates is likely to have an impact, particularly at the short-end of the curve. However, we believe there is likely to be sufficient demand from UK institutions to dampen the potential for real yields to rise.

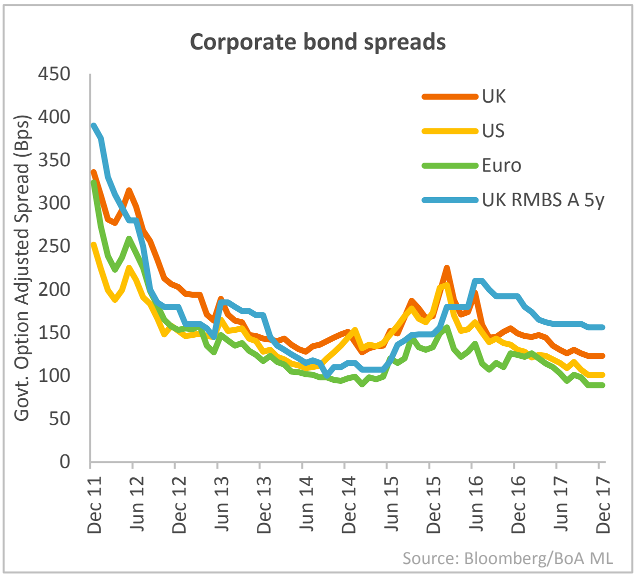


Investment Grade Credit

ML Non-Gilts Spreads over Gilts (Source: Datastream)	Sterling Non-Gilts (bps)	Sterling Non-Gilts Over 10 Years (bps)	Global Broad Market Corporate (bps)
30 September 2017	103	106	119
31 December 2017	101	107	117
Median spread over last 10 years	155	134	175
Average spreads over last 10 years	171	152	203

Note: Spreads on financials, non-financials and the broad corporate market are calculated using iBoxx indices. All other spreads are calculated using Merrill Lynch indices.



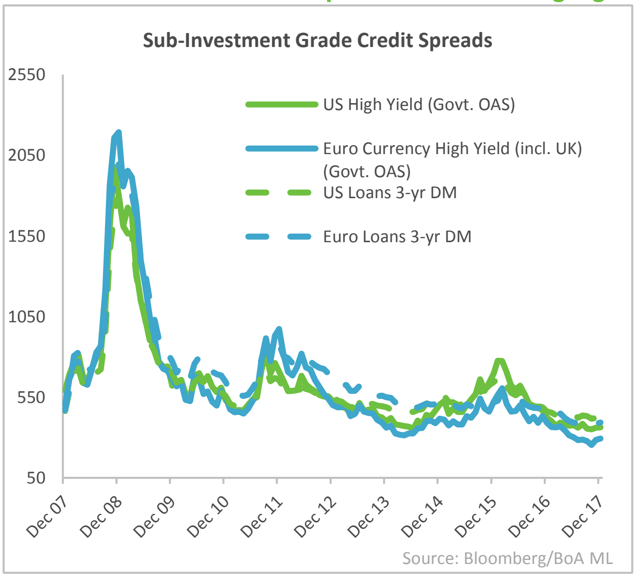


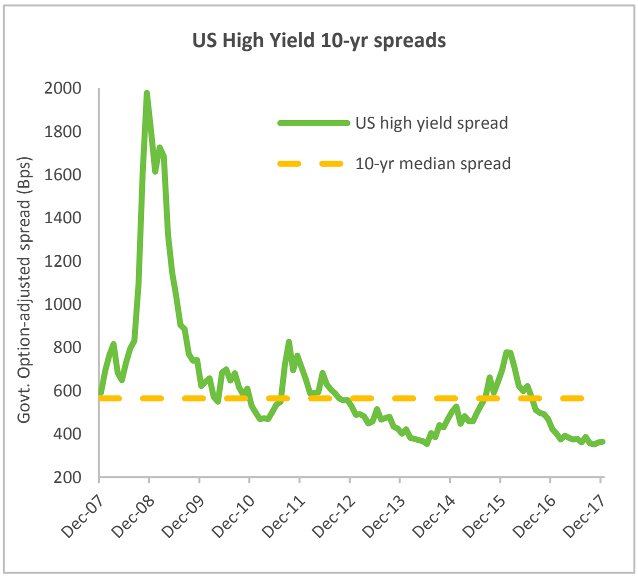
Corporate bonds capped an impressive year with another positive quarter. Current global economic momentum remains a positive for corporate bonds, but marginally tighter spreads over the final quarter has left valuations below longer-term averages. At current levels, room for further spread tightening is limited, leaving coupon income as the main source of return. Absolute yields are also unattractive given the low starting risk-free rate. We note that UK credit spreads offer a slightly higher premium over the US and Europe, but Brexit uncertainty is likely to maintain this premium.

While corporate bonds may look expensive, corporate fundamentals remain reasonably supportive. The ECB and BoE have both shifted to a dovish stance and markets are pricing in a gradual rate hiking by the Federal Reserve. Whilst the macro-economic background remains robust the fundamental background should support current spreads.

Technicals are currently supportive for corporate bonds as the carry trade remains compelling. However, although the ECB will continue to purchase bonds until September 2018, market focus has moved on to the potential impact on spreads of the eventual withdrawal of this technical support. The ECB have left their options open on the timing of any eventual withdrawal, anxious that tapering will not prove to be disruptive. Looking forward, issuance will be an important factor in 2018 as central banks buying fades.

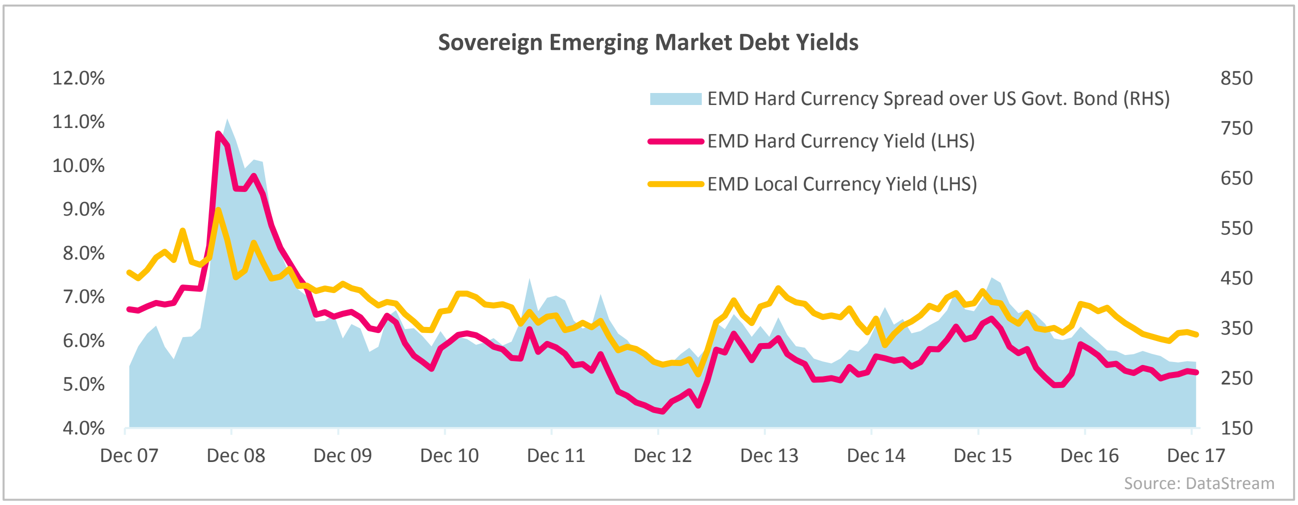
Sub Investment Grade Corporates and Emerging Market Debt





Company-specific disappointments from a few major issuers caused a wobble in the high yield market, but sentiment recovered quickly. Despite significant spread compression over the year, corporate fundamentals remain firm as the strong earnings trend continues. Default levels remain below historic levels in Europe and are improving in the US as conditions in the commodity sector continue to improve on the back of sustained price rises, particularly within the energy sector.

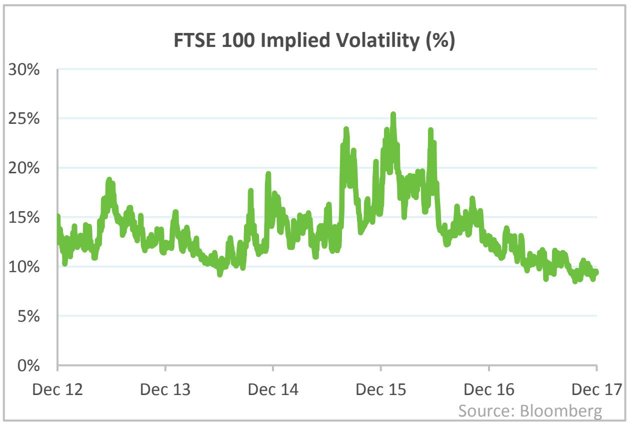
The strength of demand has resulted in further erosion of the level of covenant protection in traded bond and loans markets. We see relative value in traded loans over high yield reflecting that this market has lagged in 2017 and is offering a spread premium over the high yield market. Overall, we have a preference for private markets, where better protection can be negotiated. This market, in general, has continued to benefit from stricter covenants than those available in the traded market (where the market is now predominantly covenant-lite); this fundamentally increases the credit quality of the loans held by increasing recoveries.

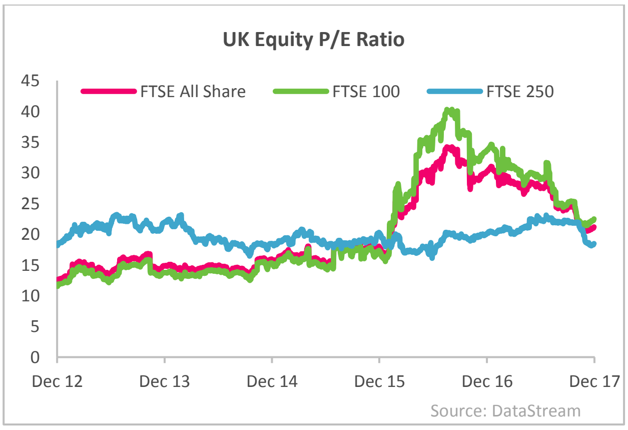


Emerging market debt (EMD) had a mixed quarter, although delivered impressive returns for the calendar year. While EMD would struggle in the short term if economic conditions deteriorate, on a longer perspective yields still look much less stretched in absolute terms than most other bond markets.

UK Equity Market

Equity Market Data (Source: Datastream)	30 September 2017	31 December 2017
FTSE All Share Dividend Yield	3.7%	3.6%
Dividend growth over the quarter	3.2%	1.7%
Dividend growth over the year	14.7%	12.8%
FTSE All Share P/E Ratio	24.4x	21.2x
Total Return during the quarter	2.1%	5.0%
Total Return over the last 12 months	11.9%	13.1%

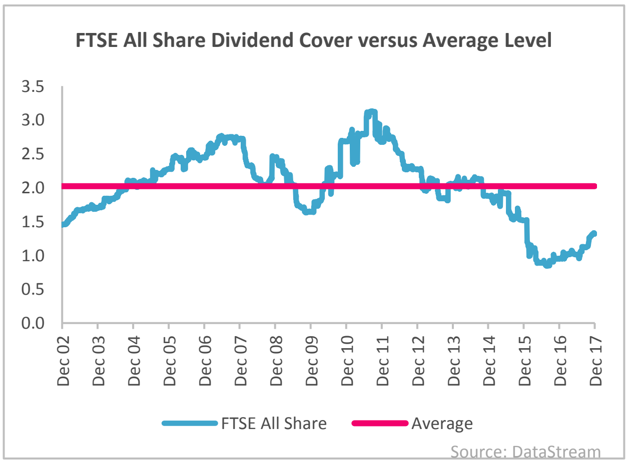


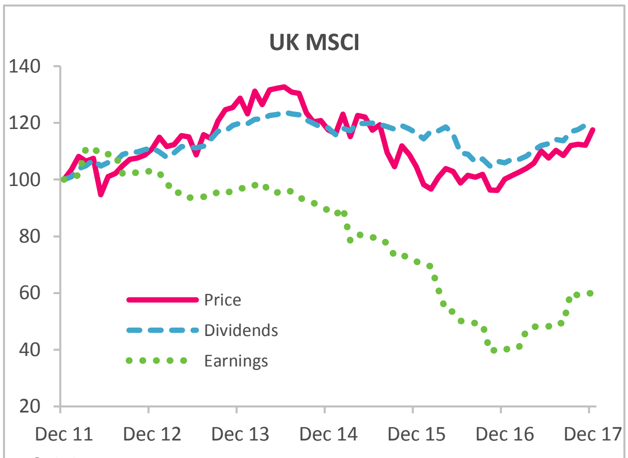


Impressive returns from mining and oil companies helped UK equities finish the year strongly, with the FTSE All Share Index delivering a return of 5% over the quarter.

Whilst global equity prices and earnings have tracked each over 2017, the resurgence of UK earnings has outstripped prices resulting in UK P/E ratios moving more in line with the rest of the world. That said, UK equities still look expensive relative to historic levels. As earnings struggled for a few years until late 2016, the main justification advanced for equity revaluation was the fall in bond yields. But global bonds yields have been rising since the middle of 2016 are now back to the levels of two years ago. Meanwhile, almost none of the equity revaluation has unwound.

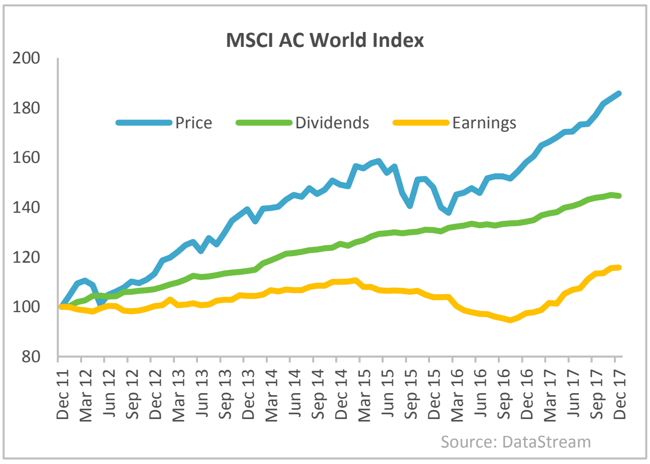
Low implied volatilities may mean that structured equity and outright downside protection can provide the opportunity to implement protection strategies relatively cheaply for those who wish to retain some exposure to potential short-term upside in equities.

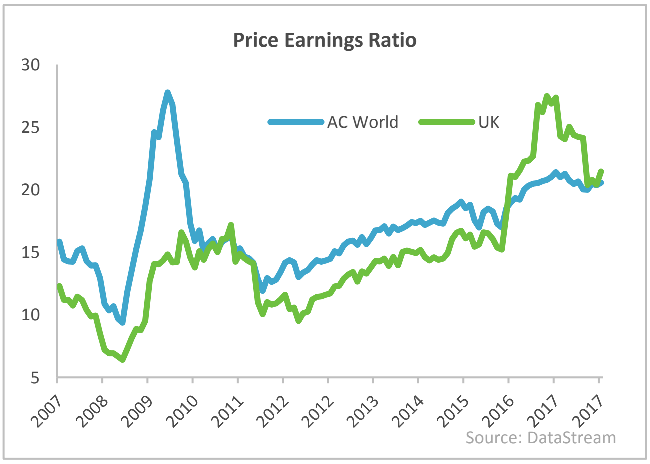




Overseas Equity Markets

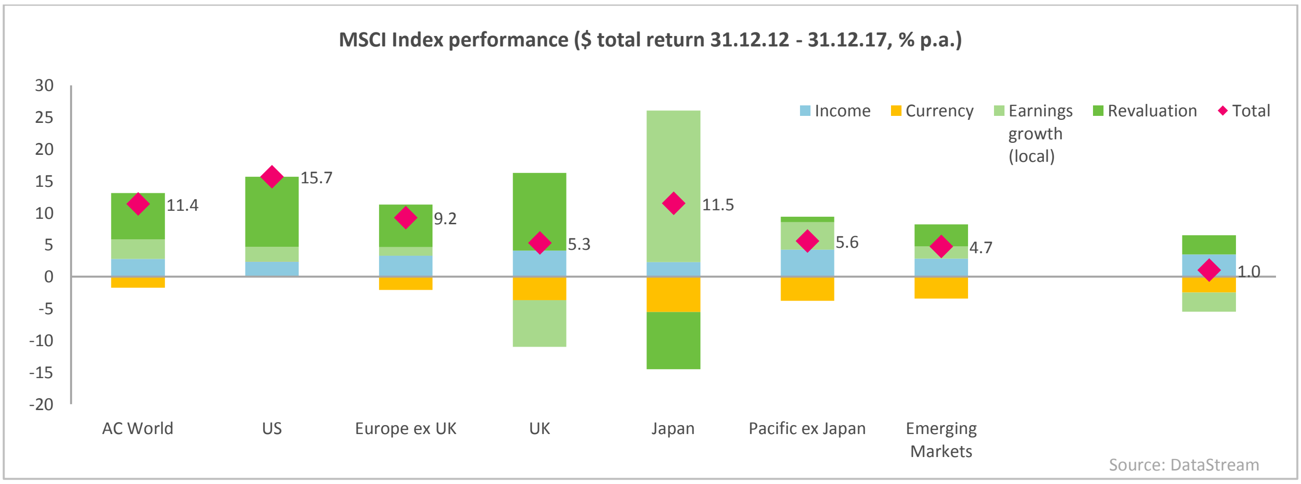
Equity Market Data (Source: Datastream)	30 September 2017	31 December 2017
Dividend Yield	2.4%	2.3%
Total Return during the quarter (£)	1.9%	5.1%
Total Return during the quarter (Local)	4.4%	5.6%
Total Return over the last 12 months (£)	15.5%	13.8%
Total Return over the last 12 months (Local)	19.1%	20.3%



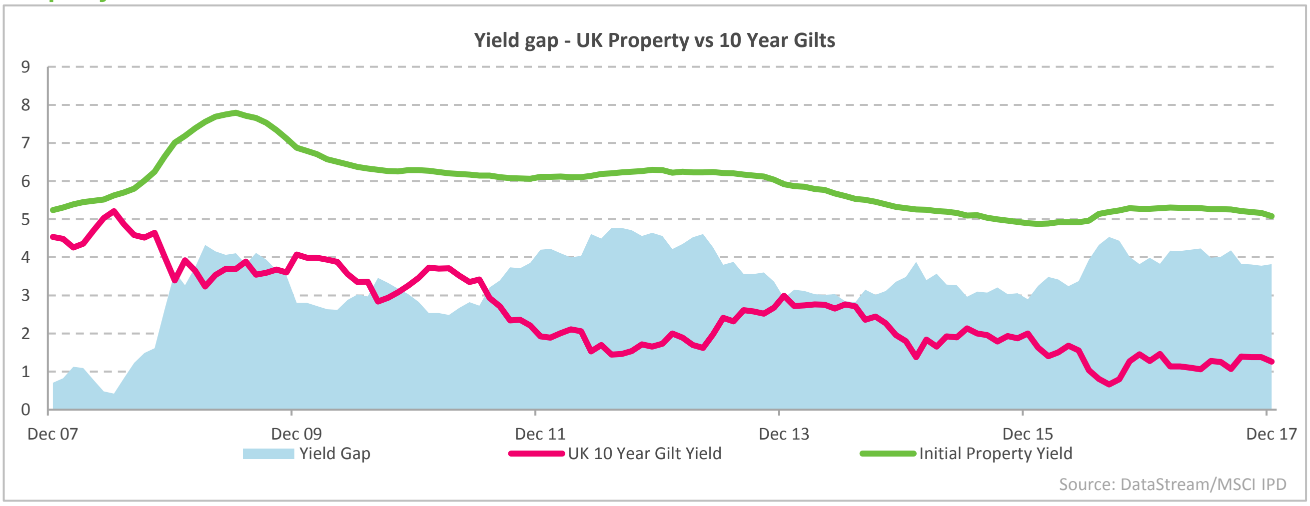


Synchronised global growth and relatively low levels of inflation provided a supportive backdrop for global equities over the quarter, delivering a return of 5.6%. Investor sentiment has been boosted in the short-term by the passing of the US tax reforms, however this may be tested as the Federal Reserve continues to unwind its QE program.

Earnings growth continues to emerge although equity valuations remain high relative to history. Momentum could easily push equities higher in the short run – it is not difficult to find examples of greater exuberance in the past – however, the longer-term outlook continues to concern us. There remains pockets of relative value across regions, with Emerging Markets and Europe looking particularly attractive relative to the US.



Property



UK Property

The post-referendum recovery in commercial property remains in place. Indeed, growth in capital values has extended the very modest acceleration evident throughout 2017. Rents are still rising modestly, although it is more difficult to detect any acceleration here. Some sub-sectors, prime industrial in particular, are experiencing higher rental growth due to tight supply whilst other sectors continue to be burdened by structural vacancies e.g. High street retail outside of Central London.

Infrastructure

Infrastructure assets with contractual, inflation linked income have the ability to provide somewhat predictable income based returns. The secure income becomes increasingly attractive as inflation ticks up. Even assets with income correlated to GDP can have reasonably predictable cash flows due to the essential nature of services provided. Infrastructure markets are underpinned by a significant need for reinvestment in aging infrastructure in developed economies and by continued global growth. Whilst there may be uncertainty on the sustainability of growth, infrastructure spending is essential to support future economic growth and infrastructure assets are defensive by nature so should be more immune to any tail off.

Notes and Risk Warnings

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets.

Exchange rates may also affect the value of any investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.

Private equity investments, whether held directly or in pooled fund arrangements carry a higher risk than publicly quoted securities; the nature of private equity pooling vehicles makes them particularly illiquid and investment in private equity should be considered to have a long time horizon.

Hymans Robertson LLP has relied upon third parties and may use internally generated estimates for the provision of data quoted, or used, in the preparation of this report. Whilst every effort has been made to ensure the accuracy of such estimates or data, we cannot accept responsibility for any loss arising from their use