Investment Advisory Committee (IAC) Quarterly Meeting

Minutes Of Meeting

Date
3/3/2016

Present members
Julius Pursaill (Chair)
Colin Taylor
Ewan Smith
Rachel Elwell
Andrew Carter
Isobel Langton

In attendance
Robin Herd
Robert Dundas
Natasa Margariti
Lorna Blyth
Ryan Medlock
Piers Hillier
Trevor Greetham
Robert Whitehouse
Peter Dorward (on behalf of RLIGC)

Owner

1. **REVIEW OF PREVIOUS MINUTES**
The minutes of the 1 December 2015 meeting were approved.

2. **PROJECTS**

Strategic asset allocation review

A paper was submitted providing further update on the proposals to change the investment strategy underlying the GPs, addressing specific questions the IAC had raised about the impact of the changes on customers. The paper focused on how the portfolio benchmarks would be adopted, the material differences between the current and proposed allocations and the process for ongoing monitoring. The paper also included proposals for modelling of the new asset classes going forward.

The IAC agreed that their questions were addressed sufficiently and were supportive that the changes could proceed subject to implementation and operational approval. The proposition team is now working to implement the changes during 2016 subject to business approval. IAC also commented that they would like visibility of the transition plan for implementation as well as details on the communication strategy for the changes. RD/LB

Fund range improvements

A paper was presented detailing how the RLP fund range could be adapted against a backdrop of customer investing with an outcome-based approach . The IAC noted that further research is required to understand the market dynamics and how the fund range might change in terms of structure and communication.

3. **Independent Governance Committee**

Peter Dorward attended on behalf of the Royal London Independent Governance Committee (RLIGC) to provide an update. The RLIGC are comfortable with the work done to date to provide transparency around transaction costs within the various group pension propositions RLG offer to customers. They acknowledged that significant progress needs to be made by the fund management industry to report fully on costs but were currently hampered by a lack of clear regulation and reporting framework within the industry.

PD expressed formal thanks for the work done by the RLI proposition team.

IAC confirmed that they had reviewed the work done by RLI to assess whether the current RLI investment default remains suitable for the workplace pension scheme members and would continue to do this on a regular basis.

4. **CUSTOMER INVESTMENTS**

STRATEGIC ANALYSIS

Governed Portfolios & Managed Strategies
No changes are recommended to the Governed Portfolio and Managed Strategy benchmarks this quarter. Governed Portfolios 3 & 6 efficiencies have improved and, whilst still outside the desired target the expected real return difference is very small so the IAC was comfortable that no change was necessary.

Governed Retirement Income Portfolios (GRIPs)
No changes are recommended to the GRIP strategic benchmarks this quarter. All the portfolios continue to be within their short term risk targets with the exception of GRIP5. Due to a slight deterioration in 10 year index linked bonds, which is used as the long term risk metric benchmark, GRIP1, GRIP2 and GRIP5 are outside of their long term risk target range. This suggests that these portfolios may not be taking enough risk. However, the IAC continue to be comfortable that no change was necessary as this measure is expected to fluctuate in the current market circumstances and to bring the portfolio back within target would involve increasing the risk being taken which was agreed to not be appropriate. The IAC will continue to monitor these metrics ahead of initiating a review of the GRIPs similar to the strategic work recently done in the GPs.

Lifestyle Path Analysis
Each Governed Lifestyle Strategy continues to be appropriate for its risk profile and investment objective.

TACTICAL ANALYSIS

Governed Portfolios & Managed Strategies
All portfolios remain within their tactical risk budgets.

There have been two tactical changes since the last meeting in November and January. The first change was effective as of 19/11/2015 and moved to a more overweight position in Gilts at the expense of Equities whilst reducing the underweight position in Index Linked Bonds.

The second change was effective as of 14/01/2016 and moved to a more overweight position in Equity at the expense of Gilts whilst further reducing the underweight in Index Linked Bonds and increasing the underweight in Property.

The overall position within the portfolios is overweight in Equities, High Yield Bonds and Gilts with underweight positions in Index Linked Gilts, Investment Grade Corporate Bonds and Property.

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Short term tactical view of the Chief Investment Officer

PH reviewed Q3 2015 and presented RLAM's rationale for the current short term tactical view:

Positioning
- Over Q4, the portfolios maintained their overweight stance in Equities at the expense of Credit and Index-linked Gilts, with a broadly neutral stance in Property. Within equities, Japan and Europe remained our preferred markets as their central banks continued to pursue very loose monetary policies. Against this, we remained underweight the UK with its high exposure to resource stocks, and Asia Pacific ex-Japan which is most negatively affected by a rising US Dollar and slowing Chinese growth

Q4 Market Background
- Global markets finished higher but remained volatile during the fourth quarter as stable to improving economic fundamentals within the US, Europe, and Japan

weighed against continued economic weakness in China and other emerging economies

- The quarter started with a recovery in risk assets on the back of a stabilisation of market conditions within China and the US Federal Reserve's decision in September to keep interest rates unchanged. Additional support came from policy easing by the People's Bank of China, strong US employment figures, and suggestions from the European Central Bank that they could add to their current stimulus program
- The rally proved short-lived as markets reversed in December amid rising credit spreads and ongoing commodity price weakness. Despite these concerns, the US Federal Reserve raised interest rates in December, marking the end of an approximately seven year period of zero interest rate policy
- Amid this backdrop, global equity markets finished the quarter higher with emerging markets continuing to lag developed markets as commodities extended their downward trajectory with energy, base metals, and precious metals all trading lower
- Within currencies, Sterling weakened across the board as the prospects of UK rate hikes receded on softening economic data and uncertainty surrounding the outcome of the European referendum. The US Dollar strengthened against most major currencies as investors priced in increased policy divergence between the Fed and other major central banks
- The UK Property market ended the year strongly with 2015 transaction volumes hitting an all-time record. Occupier demand remained healthy and a shortage of supply in the prime end of the market continued to push up rental levels, particularly in the Office and Industrials sectors

Relative Positioning & TAA Performance

- TAA positioning was a strong driver of outperformance in Q4. The largest contribution came from the overweight position in Equities, which delivered almost 7% over the period, closely followed by the underweight in Index-linked Gilts which declined during the quarter
- Within Equities, our preference for overseas markets, focussed on Japan and Europe ex-UK, at the expense of the UK and Asia Pacific ex-Japan, generated additional outperformance
- The underweight Fixed Income position turned into a strong positive contributor over Q4 as long bond yields backed up from the lows reached during Q3
- A marginally underweight stance in UK Property, which was the best performing asset class over 2015 as a whole, had a small negative allocation effect. Returns were led by the Office sector which saw significant yield compression and increased rental values, whilst Industrials enjoyed another strong year on rising occupier demand and accelerated rental growth

Outlook & Views

- Risk assets suffered one of their worst starts to a calendar year on fears of a collapse in China's growth rate and slumping oil prices hurting oil producers, in particular the emerging markets and their financial creditors. Furthermore, a slowdown in US Q4 GDP coupled with a weak manufacturing sector, fuelled fears over the outlook for the global economy

- Our base case is that China's economy is in the midst of a soft landing as it transitions from investment to consumption led growth. US growth is expected to recover from a recent dip led by consumption growth supported by a strong employment market and falls in oil prices. Furthermore, central banks are now signalling further policy easing in the face of market volatility, and declining growth and inflation expectations, which could lead to a synchronised growth upswing through 2016
- We believe this combination of loose monetary policy and muted inflationary pressures continues to provide a friendly backdrop for equities and we remain overweight accordingly. We are staying underweight Fixed Income, as we see upside risk to current yield levels as growth and inflation expectations recover in our base case scenario
- After three strong years, parts of the UK Property market are now looking expensive. Although we expect market activity to slow on uncertainty over the European referendum, the economy is expected to remain resilient as employment continues to impress and incomes grow in real terms. We will be maintaining a broadly neutral tactical stance on Property.

6. ROYAL LONDON FUND REVIEW

Governed Range

The following funds/portfolios were discussed:

Governed Range – All of the Governed Portfolios and GRIPs outperformed their benchmarks in Q4 which means all portfolios continue to outperform over both 1 and 3 years. Relative performance has improved since the last quarter over 12 months to the end of December 2015. This has been helped by strong relative performance from the underlying components of the portfolios.

RL Pension funds

The following funds were identified as requiring further discussion through the performance reporting but no action was required:

Global Index Linked
The fund suffered a bad quarter and underperformed the benchmark by 1%. This has resulted in the fund marginally underperforming over 1 and 3 years but is outperforming over 5 years.

UK Government Bond
The improvement in short-term performance has continued this quarter which means the fund is now outperforming over 1 year. This has also improved the long-term figures and the fund is now only marginally underperforming over 3 and 5 years.

UK Mid Cap
The fund suffered a really poor Q4 and is underperforming by -4.7% over one year. It is marginally underperforming over 3 years but outperforming over 5 years.

Externally Managed Matrix Funds

The following funds are subject to further action before the next quarterly IAC meeting:

Fidelity American
Another poor quarter for the fund means the significant underperformance over 1, 3 and 5 years continues. Over the short-term, the fund has suffered from its overweight position in energy stocks. Stock selection within healthcare, materials and consumer discretionary sectors have also had a detrimental effect on the relative performance of the fund.

Q4 was the first full quarter managed by the new manager, Aditya Khowala. Aditya's investment approach is to find companies that will benefit from long-term growth trends and has continued transitioning the fund since he took over from Peter Kaye. RLI have a meeting scheduled with the team at Fidelity in March and will seek reassurance regarding the way this fund is managed and to gain comfort that fund performance should improve. RH

Schroder Core UK Equity
The fund suffered another bad quarter and continues to significantly underperform over 1, 3 and 5 years.

Reflecting the poor long term performance, Schroders have communicated that they are making changes in early 2016 to the way the fund is managed. Schroders are moving the fund to be managed within their Core European Equity team with David continuing as the lead manager. This transition aligns the fund to a well-regarded team approach with a strong existing track record of delivering alpha within a team environment.

Performance will be monitored over the next six to twelve months to ensure the changes deliver positive value within the fund. RH

The following funds were discussed and will remain on watch, but no action was required:

JPMorgan US
Fund performance has improved over the last quarter and despite the fund continuing to underperform over 1 and 5 years, it is now outperforming its benchmark over 3 years. Stock selection within materials, consumer and healthcare sectors have all hurt short-term performance but the fund has benefited from stock selection in IT and energy sectors.

Invesco Perpetual Japan
The fund's performance has worsened over Q4 leading to underperformance across all time periods. The fund has delivered strong absolute gains however it is trailing the benchmark. The fund has particularly been hit by large overweights in financials and

utilities and stock selection within these sectors as well as consumer discretionary and industrials has been poor.

It’s worth noting that the contrarian nature of the manager's approach combined with a strong valuation emphasis means that returns can be volatile and there will be periods of underperformance in this fund.

Other external funds

The following funds were discussed and will remain on watch, but no action was required:

Fidelity Moneybuilder Income
The fund marginally underperformed in Q4 which has caused it to trigger as it now underperforms over 1 and 3 years. However, it is outperforming over 5 years.

Investec Cautious Managed
The fund has suffered two quarters of poor performance which has led to a further decline in the long-term performance figures. The fund is significantly underperforming over both 3 and 5 years.

Growth and momentum investment strategies have been in favour in recent years, and mid- and small-cap stocks have outperformed. This has not favoured the fund manager’s value, contrarian equity investment style, focused on large-cap stocks. The Fund remains defensively positioned to navigate through the market volatility.

Investec Emerging Local Currency Debt
Performance continues to be poor on this fund having had another quarter of underperformance. This fund is a thematic fund for specific investors looking for long term exposure to the asset. We would look for performance to gradually improve over the longer term.

Investec Global Energy
The fund’s performance improved over Q4 and actually outperformed the benchmark. This has marginally improved performance over 1 year but continues to significantly underperform over 3 and 5 years.

Given the precipitous fall in the oil price over the short-term, the exploration and production positions were responsible for most of the underperformance experienced in the fund. 2015 proved to be a second difficult year for the fund as Opec continued to put pressure the oil market. The New Year starts with sentiment at a very low ebb, but with fundamentals tightening. At some stage this year, fundamentals are expected to turn sentiment around, and the oil price start to surprise to the upside; the fund is positioned to take advantage of these market developments.

Jupiter Ecology
Fund performance has improved over the quarter and 1 year figures. We would look for this trend to continue before removing from watch.

Jupiter Financial Opportunities
The fund outperformed its benchmark for the second successive quarter and continues to outperform over 1 year. However, the fund continues to suffer over the longer-term

and is underperforming over 3 and 5 years.

The fund's holdings in exchanges and index providers continued to contribute positively towards the fund's performance. The fund's holdings in retail banks within the Eurozone detracted from performance in the quarter, in part due to the extension to the European Central Bank's quantitative easing program.

Jupiter Merlin Worldwide
The fund outperformed its benchmark again during Q4 and is outperforming over 1 year. The longer-term performance has marginally improved but is still underperforming over 3 and 5 years.

The fund remains 100% invested in equities and has further reduced its exposure to the global mining and energy sectors which has contributed to positive performance.

Legg Mason US Smaller Companies
Short-term performance has marginally improved but the fund continues to significantly underperform over all time periods.

2015 was a particularly disappointing year for the fund falling more than 8% relative to the benchmark. Individual trades in specific stocks within financial and information technology detracted most from performance as well as an overweight in energy and underweight in health care sectors. This fund focuses on quality business models and valuation discipline which was an unrewarded strategy in the US small cap market in 2015. The stocks that performed well last year were typically names that this fund would never invest into given its focus. The manager predicts that the type of market recently experienced will not prevail in 2016 and they have already seen some performance come back in early 2016 as the market shifts back to rewarding quality.

M&G Global Basics
This fund continues to underperform against a market where this investment style is out of favour. This fund is thematic in nature and we would look for performance to improve when markets support this type of theme.

M&G Global Dividend
This fund does not yet have a 3 year track record but is significantly underperforming over the short-term. Relative performance has improved compared to the previous quarter but is still underperforming and down by 10.5% over 1 year.

2015 has been a very difficult year with the fund's underperformance driven entirely by the cyclical 'assets' category which represents about 30% of the fund. Our energy-related holdings, which account for 20% of the fund, were responsible for the majority of the underperformance.

M&G Global Leaders
The fund had a good quarter and comfortably outperformed its benchmark. However, it's marginally underperforming over 1 year and significantly underperforming over 3 years. It doesn't have a 5 year track record.

The fund enjoyed good relative performance in 2015, despite 'value' stocks remaining out of favour relative to the 'growth' stocks. A further headwind was caused by the fund's overweight exposure to small and mid-cap companies which underperformed and underweight position in mega-caps which outperformed.

M&G High Yield Corporate Bond
The fund had another quarter of marginal underperformance which now means it's underperforming over 1 and 3 years. The fund has returned in line with the benchmark over 5 years.

The fund has only just triggered so we will review again next quarter and if it is still triggering, feedback will be sought from M&G.

M&G Recovery
The fund's performance worsened over the last quarter which has caused greater underperformance across all time periods, significantly over 3 and 5 years.

The fund had a difficult six months as risk aversion, together with some stock-specific issues, hit performance. The market was very unforgiving and any company that did not meet investors' expectations was severely punished. Almost 20% of the underperformance came from our underweight to the defensively focused consumer goods sector, such as drinks and tobacco companies. Overall, the biggest hit to performance came from the holdings in the healthcare sector (within biotechnology) where the fund is overweight.

Neptune Balanced
The fund did outperform its benchmark over Q4 which has improved the short-term performance. The fund, however, is still underperforming over 1,3 and 5 years.

The fund is still suffering from weak performance in 2012 and in 2014. Over 12 months, the Fund's underperformance was primarily attributed to the volatility within Chinese equities during Q3. This was because Japanese global multinationals – in which the Fund is overweight – have significant exposure to the emerging markets.

RLI held a conference call with Robin Geffen at Neptune to discuss fund performance and positioning going forward. Neptune discussed the poor performance in 2012 and the changes that have been made since then to the way the funds are managed. This has created a better culture within the team and a more direct alignment between reward and performance. We will continue to keep the fund on watch and provide further updates at future meetings.

Neptune Global Equity
The fund had a good quarter but is actually now underperforming over 1 year in addition to 3 and 5 years. The fund is significantly underperforming over 5 years.

The underperformance over five years is a result of the fund's large emerging markets weighting in 2012. This saw the Fund underperform by 11% in 2012. However, in April 2013 a number of changes were made to the portfolio – shifting the portfolio's focus to the US and Japan – since which performance has stabilised.

Refer to comments for Neptune Balanced for details of the call held between RLI and Neptune. We will continue to keep the fund on watch and provide further updates at future meetings.

Neptune US Opportunities
The fund suffered another poor quarter underperforming the benchmark. Relative

performance has improved over 1 and 3 years but is still underperforming over both time periods. The fund does not yet have a 5 year track record.

The fund's short-term performance has been hampered by the fund's holdings in financials and telecommunications sectors. Going forward, the fund will be retaining an underweight in the energy sector which has started to prove to be positive for relative performance.

Newton Balanced
Fund performance has improved over 3 month and 1 year. Historical performance continues to affect the longer term track record however Newton are seeing significant traction on this fund in the market as they are dedicating marketing support.

Newton Real Return
The fund marginally outperformed in Q4 and there has been a marginal pick-up over 1 and 3 years. However, performance over 5 years has actually worsened.

2015 saw the Fund capture a significant portion of the return generated by global equities, while avoiding the sharpest declines in global equity markets, highlighting its credentials – namely its ability to preserve capital and reduce volatility, while generating long-term growth.

Schroder Global Property Securities
The fund marginally underperformed this quarter which has resulted in underperformance over 1 year. The underperformance over 3 and 5 years is more significant and has worsened since the previous quarter.

Similar to other funds were a fundamental quality driven approach is taken, this strategy has failed to reward the fund. The manager prefers to take a longer term view and not embrace the herd mentality that has been prevalent in recent markets. This fund was brought back into Schroders in-house team last year after ending the previous joint venture.

Schroder Income Maximiser
The fund underperformed in Q4 and is now underperforming over 3 years in addition to 1 and 5 years.

The manager commented – "The past few months have been difficult for value investors, with the prevailing market environment one that has rewarded companies that have demonstrated short-term earnings growth – irrespective of their valuations and longer-term prospects. We continue to look for companies with the largest potential for dividend and capital growth, and take an active approach in applying our income enhancement strategy."

This is illustrative of the point for many funds that in 2015 managers struggled to outperform the market activity where short term gains were sought at the expense of fundamentals.

Schroder Managed Balanced
The fund has underperformed over Q4 and is underperforming over 1 year. It is marginally underperforming over 3 years but is outperforming over 5 years.

The fund has only just triggered so we will review again next quarter and if it is still triggering, feedback will be sought from Schroder.

Threadneedle Absolute Return Bond
The fund has had a horrible quarter and is underperforming now over all time periods.

The fund has only just triggered so we will review again next quarter and if it is still triggering, feedback will be sought from Threadneedle.

Threadneedle Latin America
The fund had a good quarter and outperformed the benchmark but remains an underperformer over 1, 3 and 5 due to historical poor performance.

At a sector level, financials, consumer staples and materials has contributed to returns over the short-term. On the other side, utilities, industrials and healthcare stocks lagged.

UBS Global Blended
The fund had a better quarter than the previous one and returned in line with the benchmark. However, the fund is still underperforming over 1, 3 and 5 years. The better performance in Q4 has marginally helped the fund and we would look for this to continue into 2016.

The following funds have improved and are no longer on watch:

JPMorgan Natural Resources, JPMorgan New Europe.

7. DATE FOR NEXT MEETING

The next quarterly meeting is 14th June 2016.

IMPORTANT INFORMATION

Past performance is not a guide to the future. Prices can go down as well as up. Investment returns may fluctuate and are not guaranteed so you could get back less than the amount paid in.