Canal & River Trust

REPORT TO CANAL & RIVER TRUST COUNCIL

PROPERTY AND INVESTMENT

Report by Stuart Mills, Director of Property
March 2015

1. Introduction

On formation, Government gifted a portfolio of investment assets to the Trust, the income from which would help to fund the waterways into the long term.

At the time, these assets were largely property or property-based assets (eg, shareholdings in property joint ventures) held by British Waterways Board.

The Grant Agreement sets out some high level principles as to how the investment assets should be managed by the Trust moving forward and provides for the Trustees to adopt a Group Investment Policy (GIP) to set this out in more detail.

2. Group Investment Policy

The Trustees approved the Group Investment Policy (GIP) for the Trust during 2014. The GIP sets out how the Trust will manage its investment assets to comply with the Grant Agreement and is attached for information as Annex 1.

A fundamental principle which is detailed in the GIP is the intention to diversify away from a pure property portfolio of investment assets whilst maintaining a significant proportion of the assets in property. This would provide an element of risk protection which would not be afforded by investment in one sector alone.

3. Investment Performance

A presentation will be made to the meeting to provide an update on progress with the GIP and the performance of the overall portfolio of investment assets.

Stuart Mills
Director of Property
11 March 2015

ANNEX 1

STATEMENT OF GROUP INVESTMENT POLICY FOR THE CANAL AND RIVER TRUST ("Trust")

July 2014

Contents

Preface. This Group Investment Policy ("GIP") documents the investment strategy for the Trust's Investment Assets (as defined in Clause 1) and the policies that will guide investment decision-making. It is designed to provide parameters within which the Investment Assets will be managed. The Trustees have delegated the power to authorise investments, subject to the limits set out in this document, to the Investment Committee ("IC"). The Protector and the Trustees shall review this document as required but generally no more frequently than three yearly. Material changes must be ratified by the Trustees of the Canal & River Trust (the "Trustees").

Definitions:

1.1 The following definitions are quoted from the Grant Agreement between the Trust and Defra dated 28th June 2012 ("Grant Agreement").

1.1.1 The Investment Assets comprise all the assets transferred to the Trust (and its subsidiaries) other than those assets held in the Infrastructure Property and the Protected Operational Assets.

1.1.2 The Infrastructure Property comprises the permanent endowment of infrastructure property relating to the inland waterways established by the Trust Settlement (known as the Waterway Infrastructure Trust).

1.1.3 The Protected Operational Assets comprise property that is used to facilitate the effective management and operation of the infrastructure, held by the Trust under the Trust

Settlement, but which does not form part of the Infrastructure Property and includes property or assets of historical, architectural, engineering, amenity or environmental value or merit that the Trust considers desirable to hold or retain without the need to provide an investment return to the Trust.

1.1.4 The Protector shall monitor the management of the Investment Assets in order to detect any actual or threatened Material Diversion or Material Diminution. The Protector will receive the Annual Investment Plan setting out the Trust's plans for investment in each year for comment.

1.1.5 A Material Diversion comprises a material diversion from the Agreed Purposes (see below). A Material Diminution comprises a diminution in the value of the Investment Assets, other than due to unavoidable market fluctuations, which is sufficient to materially impair the capability of the Trust to discharge its duties under the Trust Settlement in the short or long term.

1.1.6 The Protector means the person appointed to monitor compliance under the Protector arrangements of the Grant Agreement pursuant to clause 13 and schedule 8.

2. Introduction

2.1 This statement comprises the GIP required under Schedule 8 of the Grant Agreement with Defra dated 28th June 2012.

2.2 The Trust, a charitable company limited by guarantee, was formed pursuant to the Public Bodies Act 2011, British Waterways Board (Transfer of Functions) Order 2012 under which the functions and property relating to the waterways in England and Wales have been transferred from British Waterways Board ("BWB") to the Trust.

2.3 The main objects of the Trust are to preserve, protect, operate and manage Inland Waterways for public benefit:

- for navigation;
- for walking on towpaths; and
- for recreation or other leisure-time pursuits of the public in the interest of their health and social welfare.

2.4 Part of the property transferred to the Trust comprises an endowment of Investment Assets which at the time of transfer were predominantly property, or property related investments ("Property and Joint Venture Investment Assets"). The Investment Assets have been used by BWB to generate income and profits that have been used to support the maintenance, operation and management of the waterways.

2.5 The Grant Agreement clearly defines the Investment Assets and provides for the income arising from those assets to be applied to the Agreed Purposes, (see section 3 below). The Grant Agreement also provides for the appointment of a Protector to monitor the management of the Investment Assets against this GIP.

2.6 The Trust's income is generated from a range of sources. Approximately 75% of Trust's income is generated by the Infrastructure Property comprising rents, boat licenses, mooring fees, water sales and transmissions, and other utility income. The remaining 25% of the Trust's income is generated by the Investment Assets.

3. Key Operating Principles

3.1 **Agreed Purposes.**

3.1.1 The Grant Agreement specifies that the main purposes of the Investment Assets are:

- to generate revenue to fund the maintenance and operation of the waterways, the statutory obligations of the Trust and the Trust's other charitable objects;

- to provide the Trust with a source of capital funds to address unexpected events such as infrastructure failure or the risk on imminent failure, subject to the requirement over time to replace such capital funds from other available resources;

- to provide balance sheet strength to the Trust for the purposes of fulfilling its obligations as principal employer of the Waterways Pension Fund and to provide security for any borrowings of the Trust.

3.1.2 In addition the Grant Agreement provides that "the Trust shall actively manage the Investment Assets in the context of the overall resources and liabilities of the Trust to maintain and grow without undue risk the capital value and the income return in real terms. The Trust shall, in normal circumstances, reinvest the net capital receipts from disposals of Investment Assets for long term growth in capital and revenue. The Trust shall not use the Investment Assets in any manner that is inconsistent with the Trust's objects."

3.2 Overall Investment Objectives.

3.2.1 To meet the agreed purposes, the overall investment objective is to maximize the total returns (income and capital gains) of the Investment Assets without taking undue risk over a medium to long term horizon.

3.2.2 Income from the Investment Assets is to be used to fund the ongoing maintenance, operation and repair of the waterways. Under the terms of the Grant Agreement the income arising from the Investment Assets must be applied to the Agreed Purposes (Section I, Para A) and it is the Trust's Policy not to seek to accumulate income for the purposes of increasing the capital endowment other than in exceptional circumstances (such as a large one-off revenue receipt for the grant of property rights). However, short term (2-3 years) surpluses, and deficits, may be incurred on revenue account for the purpose of managing expenditure and income volatility from year to year.

3.2.3 In addition to funding ongoing expenditure, it is desired that the Investment Assets preserve and grow their value in real terms to support increased future expenditure on the charitable activities. This objective is to be assessed over the medium to long term (5 to 10 years) such that the capital growth in those years when the growth target is not achieved may be recovered in other years where the growth target is exceeded. If the Investment Assets growth exceeds inflation (as measured by UK RPI) by 1% per annum (measured over the medium to long term) the Trust may apply all or a proportion of that excess growth to enhance the expenditure of the Trust on its charitable activities.

3.2.4 The selection of Investments Assets should not be influenced by the proportion of returns that arise from income or capital gains. Subject to 3.2.3 above the charitable activity expenditure requirements may be met from income and realised real capital growth.

3.2.5 The overall investment objective is long term and, subject to the need to realise some capital value to fund capital liabilities and charitable expenditure, the short term movement in investment values should not affect the achievement of the main investment objectives unless there is a Material Diminution.

3.2.6 The Trust shall actively manage the Investment Assets in the context of the overall resources and liabilities of the Trust to achieve these objectives. The Trust shall not use the Investment Assets, nor investment proceeds, in any manner that is inconsistent with the Trust's objects.

3.3 **Withdrawal Target.**

3.3.1 The directly held Property and Joint Venture Investment Assets will be managed by the Trust as part of its normal operations. Cash flows will pass through the income and capital bank accounts in accordance with the established procedures.

3.3.2 Investments outside the Property and Joint Venture Investment Assets ("Non-Property Investment Assets") will need to provide for an annual cash withdrawal amount to generate cash flow to fund the expenditure on the charitable activities. To facilitate the cash flow requirement a long-term spending target shall be used such that in any given fiscal year the target amount to be withdrawn from the portfolio in cash ("Withdrawal Target") shall be up to 5.0% of the average value of the Non-Property Investment Assets over a rolling five-year period, but subject to having first satisfied, and retained within the Investment Assets value, the real growth criteria in paragraph 3.2.3. This withdrawal target forms part of the return objective for the Non-Property Investment Assets. The funds withdrawn from Non-Property Investment Assets should first be taken from accumulated income reserves and secondly, subject to complying with the provisions of paragraph 3.2.3 above, from realised capital gains.

3.4 **Return Objective.**

3.4.1 The Trust's target return objective for the Investment Assets is a nominal total return of 8% per annum but subject to the requirement that the capital value of the Investment Assets shall target minimum growth of UK RPI plus 1.0% per annum (each measured over rolling ten-year periods)..

3.4.2 The Strategic Asset Allocation for the Non-Property Investment Assets (As outlined in Exhibit 1) is designed to generate a total (income and capital gains) nominal return of 8.5% (6.5% real plus UK RPI) after all management charges. This leaves a margin of 0.5% (8.5% - 8.0%) which is appropriate to build a cushion against the risk of downturns.

3.5 **Risk Parameters.**

3.5.1 The Trust's wide diversity of existing income returns, particularly from the Infrastructure Property, will help protect against a temporary or permanent loss in funding from Investment Assets however waterway expenditure cannot readily be deferred or reduced to a material degree.

3.5.2 The Trust stands prepared to incur risks consistent with its pursuit of the return objectives set forth above and as such can tolerate some short term volatility. Risks come in many forms, and the main risk the Trustees wish to avoid in the GIP is the permanent loss of value of the Investment Assets and the loss of part of the funding stream from Investment Assets, either temporarily or permanently.

3.5.3 The Trust expects to retain a significant weighting in directly held UK property for the following reasons:

- The Trust is a significant owner of operational real estate (infrastructure trust property) and wishes to continue to lever the wider long term benefits available to it arising from the synergy between the Infrastructure Trust assets and real estate endowment properties. This manifests itself in the delivery of significant Infrastructure Trust asset enhancements arising from real estate transactions (associated infrastructure works, public realm facility provision) and its ability to influence the nature of property use and development adjacent to its infrastructure assets, thus improving the overall quality of experience associated with its infrastructure assets. This closely aligns UK property investments with the charitable objects of the Trust.

- The ownership of significant infrastructure trust assets means the Trust has, and will always need, a significant in-house management capability in UK property which should be fully utilised for the benefit of the organisation. Holdings in direct UK property secure the achievement of management efficiencies through economies of scale which would not be delivered from other investment classes.
- A significant proportion of the Trust's UK property assets (circa [40%]) represent long term geared ground rental investments which are low risk, low volatility holdings and have satisfied the return objectives of the Trust over the long term. Additionally, they complement the Trust's long term role in the custodianship of the waterways for the reasons noted above.

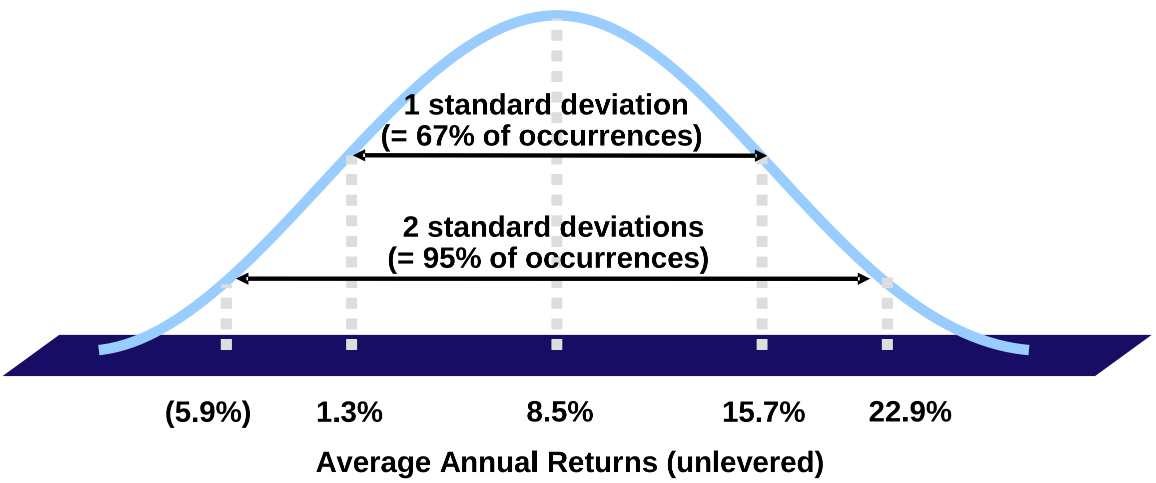
The Trust expects to continue the established trend for the performance of its Property and Joint Venture Investment Assets and aims to exceed benchmark performance (defined by the UK IPD index) over the long term.

3.5.4 Appendix 1 details the Investment Objectives & Parameters under which the Property & Joint Venture Investment Assets will be managed. This Appendix will be reviewed at least bi-annually by the Investment Committee, or more regularly should market circumstances dictate.

3.5.5 The Non-Property Investment Assets portfolio will include assets other than UK property and implementation will be through regulated or unregulated collective investment vehicles (including but not limited to private partnerships, offshore funds, mutual funds, exchange traded funds, OEICs, onshore or offshore trusts) providing appropriate written independent professional advice has been received by the Trustees in relation to each Non-Property Investment Asset. Non-Property Investment Assets shall not be greater than 40% of the Investment Assets.

3.5.6 The Strategic Asset Allocation (As outlined in Exhibit 1) embeds an expected future annual volatility measured by a 7.2% standard deviation around the mean expected return of 8.5% nominal. A 7.2% standard deviation compares favourably to the average historical standard deviation for developed market public equities of 16 – 20%.

3.5.7 For illustrative purposes, if we assume a normal distribution of possible future returns around the mean, this 7.2% standard deviation suggests a range of outcomes such that we would expect to experience two of every three years' returns falling within a one-standard deviation range of roughly +1.3% to +15.7% (nominal). Over the long term, we would expect the average annual return converges more closely to the mean and on average 19 out of 20 years can be expected to fall within two standard deviations of the mean. This is illustrated by the bell curve below.



3.6 **Liquidity.**

3.6.1 In normal circumstances it is expected that there will not be a material need for Investment Assets to be realised in cash to fund the operational expenditure. However short term cash requirements and the Withdrawal Target may be funded from either the sale of liquid assets or the use of a modest level of debt secured on the directly held property portfolio.

3.6.2 Surplus investment funds may be either: reinvested, applied to reduce debt capital or held in separate bank accounts designated "Investment Capital" and invested, in the short term, in money market investments in accordance with the Trust's Treasury Policies pending longer term investment decisions.

3.6.3 Given the relatively limited liquidity requirements the Trust may invest up to 50% of the Non-Property Investment Assets in illiquid assets, defined for these purposes as assets that cannot be liquidated for cash within 52 weeks. In addition, illiquid Non-Property Investment Assets which do not provide a regular and significant income yield shall be limited to 25% of the total Non-Property Investment Assets.

3.7 **Debt Gearing.**

3.7.1 The use of underlying asset managers that employ gearing as part of their investment strategy is allowed and is expected for at least some of the selected underlying asset managers in the Non-Property Investment Asset portfolio.

3.7.2 A modest level of gearing may also be applied at the overall Investment Asset portfolio level, or against specific assets within the Property and Joint Venture Investment Assets portfolio, for the purposes of enhancing net returns. Details of the use of debt gearing can be found in the separate [Debt Gearing Strategy document].

3.8 **Currency Management.**

3.8.1 The Property and Joint Venture Investment Assets portfolio will be located in the UK and will be denominated in UK £ sterling. Accordingly no currency risk will be incurred compared with the currency of the Trust's expenditure.

3.8.2 The Non-Property Investment Assets portfolio will be protected from foreign exchange rate fluctuations through the deployment of appropriate currency hedging strategies in order to cost effectively limit Non-Sterling currency exposures to 20% of the Non-Property Investments value. Due to the market cost of hedging, the only currencies to be hedged will be US Dollars, Japanese Yen and Euros. The currency overlays will be subject to a +/-10% variation in respect of the aggregated hedged currencies (i.e. the total US Dollar, Euro and Yen currency exposure could range -10% to +10% compared to the target level). Currency exposures will be reviewed on a quarterly basis to ensure compliance with the above targets. Where there is a trade-off between overall portfolio liquidity and maintaining the currency overlay, considerations of liquidity may take precedence.

3.9 **Taxation.**

3.9.1 As a charity the Trust is able to claim exemptions against taxation on its income and capital gains provided that they are applied to the charitable purpose. The exemptions for charities from stamp duty and stamp duty land tax are also available to the Trust.

3.9.2 Income arising from the investments will be applied to fund the waterway expenditure and as such will have been applied to the charitable purpose and should be exempted from income tax.

3.9.3 Proceeds arising from disposals of investments will need to be re-applied in full to new investments that fulfill the charitable purpose to enable any capital gains that arise on the disposal to be exempted from capital gains taxation.

3.10 **Ethical Issues**

3.10.1 The Trustees wish to adopt an ethical policy consistent with its policies in respect of other areas of its business, notably fundraising. More generally, individual investments may be excluded if they are perceived to conflict with the Trust's objects and purposes.

3.11 **Measurement Periods.**

3.11.1 The adoption of rolling ten-year periods for assessment of results reflects a balancing of the linked expenditure and return objectives set forth above with The Trust's tolerance for unexpectedly poor results. Consistent with the ten-year period for assessing results, declines in the Investment Assets purchasing power that have persisted for less than three years will not result in fundamental changes to investment strategy, unless they constitute a Material Diminution.

4. Implementation

4.1 **Responsibilities.**

4.1.1 The Executive shall prepare annually a tactical asset allocation plan for the Trust for consideration by the IC. The plan shall address the requirements of this GIP. The plan will be endorsed by the Committee and submitted to the Trustees for approval and will provide for a flexible range of investment parameters to enable the Committee to make changes to investment holdings within those parameters without the need to refer regularly to the Trustees for approvals. This is necessary to facilitate the rapid execution of transactions following market related decisions taken by the Committee.

4.1.2 The plan shall include a proposed asset allocation and an Investment Plan for each section of the assets within the allocation.

4.1.3 The Strategic Asset Allocation is set out as Exhibit 1 and represents the asset mix that is hypothetically likely to produce the return objective within the risk parameters set forth above.

4.1.4 The investment plans for each year shall be prepared by the Executive and formally reviewed on an annual basis by the Protector and modified as needed in light of experience and changing circumstances, based on research and discussion involving IC members and outside experts. Such discussion focuses on the Trust's liquidity needs and perceived risk tolerance, as well as the projected behaviour of asset classes and strategies deemed worthy of consideration for The Trust's potential use.

4.1.5 The Debt Gearing Strategy will also be prepared periodically by the Executive for consideration by IC and, when endorsed, submitted to the Trustees for approval. The nature of the debt strategy will be such that all material changes to the Strategy and the debt instruments will require the approval of the Trustees. To the extent that undrawn borrowing facilities are available to the Trust the Strategy will provide for delegated authority to the Committee to draw and repay such facilities within agreed parameters.

4.1.6 The IC should consider the gearing limit imposed on the overall levels of debt but also consider the need for interest hedging strategies, the need for phased repayment dates and the avoidance of excessive dependence on particular debt markets or providers. In addition the IC should also give consideration to appropriate long-term debt sources and arrangements to match the long-term planning requirements for operational expenditure. The Debt Gearing Strategy provides the ranges within which the IC will operate with discretion on these parameters. The IC has discretion to purchase assets or fund expenditures using borrowed money in order to avoid liquidations of Investment Assets at inopportune times as long as the portfolio remains within the limits of the Gearing Strategy.

4.1.7 Authorising commitments or bids and tenders in excess of £15m is a matter reserved to the Trustees for approval under the CRT Scheme of Delegation. The Trustees have also reserved to themselves the approval of all Strategic Plans and Policies of the Trust.

4.1.8 In addition, Article 9 of the CRT Articles of Association provides for the Trustees to delegate their powers and functions. The IC has delegated power to £15m.

4.2 **Rebalancing.**

4.2.1 Rebalancing of liquid Investment Assets will normally be undertaken on a quarterly basis to re-align asset allocations with the long-term allocation ranges. Where funds are required for operational purposes, rebalancing may be taken on a more frequent basis. Deviations from targets (but within the range) for liquid Investment Assets will reflect shorter-term tactical asset allocation views.

4.3 **Performance Reporting.**

4.3.1 The Executive shall provide to the IC a package of performance information containing financial and valuation data, compared against the Plan and benchmarks, together with information on asset allocation, gearing levels, proposed investment decisions, and any other information relating to material issues. Specifically the information shall include management accounts, cash flow forecasts, performance analysis and commentary.

4.3.2 Proposed transactions shall be submitted to the IC and the Trustees for approval in accordance with the agreed delegated authorities. Transaction reports of the activity carried out since the previous meeting together with post project appraisals shall also be submitted.

Appendix 1 to Group Investment Policy for the Canal & River Trust

Property & Joint Venture Investment Assets ("Property Assets")

Investment Objectives and Parameters

Overview

The Property Assets will be managed in accordance with the overall investment objectives set out in the Group Investment Policy.

The Investment Assets of the Trust will comprise approximately 80% Property Assets (range 60-80%).

Subject to the overall target return for the Investment Assets of 8% (set out in para 3.4.1 of the Group Investment Policy) the return objective from the Property Assets is to exceed returns from the Investment Property Databank (IPD) All Property Index (or such other suitable index to be determined by the Investment Committee) on a rolling annualised 5 year basis.

The Trust expects to retain an overall portfolio weighting as follows:

- 80% (range 70-90%) by value of Property Assets in income portfolio with a minimum total return of 8% per annum nominal.
- 10% (range 10-20%) by value of Property Assets in growth portfolio with a target total return of 10% per annum nominal. Growth assets are those where the Trust has the potential, within a 5 year period, to realise material capital growth through proactive preparatory development activity.
- 10% (range 0-10%) by value of Property Assets in equity interests in joint venture property development vehicles engaged in land trading or direct development activity. At project level, target return is equity IRR of 20%. Target return in respect of overall investment in joint venture activity is 15% equity IRR.

Control parameters for each element of the Property Assets will be subject to regular review based on market performance and other relevant investment factors.

As a minimum, all significant property assets (value > £1m) will have individual Asset Plans prepared to set out the medium term objectives and key deliverables for the asset.

Income Portfolio

The Income portfolio will be managed within the following control parameters:

Control Parameter	Metrics	Rationale
Location	No requirement for location next to waterways owned by the Canal & River Trust.	To ensure consistency of risk profile with market investors.
Sector allocation	Sector / Target Range Agricultural 0-5% Industrial 10-25% Office 15-25% Residential 0-10% Retail 5-25% Ground Rents 40-60% Other 0-5%	To avoid excessive exposure to any single market sector. Retail exposure limited to non-high street (outside Trust core competency).
Geographic allocation	[Ranges being calibrated with IPD and to be resolved by 31/3/15]	To benefit from long term strength and stability of London and South-East markets. To avoid excessive exposure to any single geographic market outside London & South East.
Freehold/Leasehold	No more than 10% of the portfolio to be invested in leasehold interests (excl ground rents on very long headleases).	To reduce exposure to wasting asset values.
Asset Concentration	Excepting long term secure ground rental assets; no individual property shall represent more than 5% of the total value of the Property Assets. Excepting long term secure ground rental assets, the top 5 properties shall represent no more than 20% of the total value of the Property Assets.	Other than in the case of long term, secure ground rents, to manage exposure to single markets, sectors or covenants.
Covenant Exposure	Excepting long term secure ground rental assets, no individual covenant shall impact more than 5% of the total value of the Property Assets.	Other than in the case of long term, secure ground rents, to manage exposure to single covenants.
Gearing	Gearing secured on the directly owned property portfolio shall be limited to 20% of the total portfolio value.	To manage exposure to market downturn.
Derivatives	No use of derivatives within the portfolio with the exception of appropriate interest rate hedging devices such as options and swaps; commensurate with gearing exposure.	Avoid use of sophisticated instruments which may contain hidden risk unrelated to core property markets.
Development prefunding with the intention of maintaining the asset within the income portfolio.	For pre-let arrangements, expected value on completion to be no more than 5% of portfolio value at any one time. For speculative arrangements, expected value on completion to be no more than 1% of portfolio value	To manage exposure to development process and third party risk.

Growth Portfolio

The Growth portfolio will be managed within the following control parameters:

Control Parameter	Metrics	Rationale
Location	Location will preferably be within vicinity of waterways owned by the Canal & River Trust.	To harness the synergy between operational real estate and the benefits of medium term regeneration and improvement through development activity.
Geographic allocation	No more than 50% of growth portfolio assets by value to be within Greater London. Outside Greater London, no more than 10% of growth portfolio assets by value to be within any single City or Town.	To benefit from long term strength and stability of London and South-East markets. To avoid excessive exposure to any single geographic market outside London & South East.
Freehold/Leasehold	No investment in leasehold interests with unexpired lease length of less than 150 years.	To ensure security for future investment.
Asset Concentration	Within Greater London, no single asset to represent more than 25% by value of the growth portfolio assets. Elsewhere, no single asset to represent more than 10% by value of growth portfolio assets.	Other than in the case of long term, secure ground rents, to manage exposure to single markets, sectors or covenants.

Joint Ventures

The joint venture investments comprise investment in corporate entities with a partner or partners and will be managed within the following control parameters:

Control Parameter	Metrics	Rationale
Location	Location of activities will preferably be within vicinity of waterways owned by the Canal & River Trust.	To harness the synergy between operational real estate and the benefits of medium term regeneration and improvement through development activity.
Recourse	No upstream recourse to CRT (either directly or via CIC) for external indebtedness of JV or for any downstream guarantees or letters of comfort.	The charity is legally unable to provide support of this kind to trading entities. Limits CRT exposure to equity investment.
Partner Exposure	Of very good reputation/record with credit availability commensurate with equity commitment. Consortiums allowed but single partners preferred	Limit reputational and financial risk. Maximise leverage from financial and intellectual assets
Decision making	50:50 voting rights with no overall control	Joint not subsidiary control.
Gearing	Decision for JV board	Should be free to access capital as efficiently as possible

Dispute resolution	Deadlock, Upward referral	No shoot outs - creates requirement to resolve issues through negotiation for mutual benefit
Structure	Tax transparent (LLP/LP)	Facilitates gift aid of pretax profits

EXHIBIT 1 – INVESTMENT ASSETS STRATEGIC ASSET ALLOCATION – [TO BE AGREED]

- The Strategic Asset Allocation is expected to generate a [8.5]% nominal annual return over a ten year period. Compared to the return objective of [8.0]%, this leaves a margin of [0.5]% ([8.5]% - 8.0%) which assumes regular rebalancing and a mature private equity portfolio
- Primary risk parameter = maintain portfolio annual volatility below [8.0]% per annum, assuming [0]% of gearing at the portfolio level

	Asset Allocation					
Segment / Eligible Asset	**Min**	**Strategic Asset Allocation**	**Max**	**Nominal 10Yr Forecast Return**	**Standard Deviation (2)**	**Benchmark**
Cash and Equivalents	**0.0%**	**0.0%**	**5.0%**	2.0%	1.0%	**3-month GBP LIBOR**
Fixed Income	**0.0%**	**1.0%**	**10.0%**			**FTSE A British Govt All Stock TR**
Gilts	*0.0%*	1.0%	*10.0%*	3.5%	6.0%	*FTSE A British Govt All Stock TR*
Credit	**3.0%**	**7.0%**	**15.0%**			**Markit iBoxx Sterling Non Gilts Overall TR**
Liquid Credit	*1.0%*	2.5%	*10.0%*	6.0%	10.0%	*Markit iBoxx Sterling Non Gilts Overall TR*
Illiquid Credit	*0.0%*	4.5%	*10.0%*	10.0%	11.0%	*Barclays Capital Global Huigh Yield TR LC*
Hedge Funds	**1.0%**	**2.0%**	**10.0%**			**HFRI FoF: Composite**
Absolute Return	*0.0%*	*1.5%*	*10.0%*	6.0%	6.0%	*3-month T-bill*
Hedged Equity	*0.0%*	*0.5%*	*10.0%*	6.0%	8.0%	*HFRI: FoF Strategic Index*
Public Equity (including hedged equities)	**2.0%**	**4.0%**	**15.0%**			**MSCI World NR LC**
Large Cap Equity	*1.0%*	*3.0%*	*10.0%*	8.0%	16.0%	*MSCI World NR LC*
Emerging Market Equity	*0.0%*	*1.0%*	*7.0%*	10.5%	24.0%	*MSCI EM (Emerging Markets) NR LC*
Private Equity	**0.0%**	**5.0%**	**10.0%**	15.0%	20.0%	**Cambridge Associates Private Equity**
Inflation Hedges (Real Assets)	**60.0%**	**81.0%**	**100.0%**			
Commodities	*0.0%*	*0.0%*	*5.0%*	5.0%	20.0%	*S&P GSCI TR*
Core Property	*50.0%*	*66.0%*	*85.0%*	6.5%	8.0%	*IPD All UK Property Monthly TR*
Development Property	*0.0%*	*15.0%*	*30.0%*	13.5%	18.0%	*IPD All UK Property Monthly TR + 500bps*
Inflation Linked Bonds	*0.0%*	*0.0%*	*10.0%*	3.5%	6.0%	*FTSE A (Index Linked) British Govt All Stocks TR*
Total Portfolio		**100.0%**		**8.5%**	**7.2%**	
Total Portfolio (20% leverage at 3.0%)				**9.6%**	**8.6%**	

Notes: (1) Minima and maxima are asymmetric by design. (2) Expected real returns and standard deviations reflect Partners Capital asset class assumptions.
(3) Inflation rate assumed to be 2% p.a.