QUARTERLY REVIEW PREPARED FOR

Oxfordshire Council Pension Fund

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PENSION FUND COMMITTEE – 1 DECEMBER 2017

OVERVIEW AND OUTLOOK FOR INVESTMENT MARKETS

Report by the Independent Financial Adviser

Economy

1. The forecast growth rate for the UK economy in 2017 has been revised downwards to 1.5% after sluggish growth in the second quarter, although the third-quarter rate of 0.4% exceeded expectations. Meanwhile, forecast growth rates in the other developed regions have been maintained or revised upwards.

(In the table below the bracketed figures show the forecasts made in August) [Source of estimates: The Economist, October 7th 2017]

Consensus real growth (%)						**Consumer prices latest (%)**
	2014	**2015**	**2016**	**2017E**	**2018E**	
UK	+2.8	+2.3	+2.0	+1.5 (+1.6)	+1.3	+3.0(CPI)
USA	+2.4	+2.4	+1.6	+2.2 (+2.2)	+2.3	+ 1.9
Eurozone	+0.8	+1.5	+1.6	+2.1 (+1.9)	+1.9	+ 1.5
Japan	+0.3	+0.6	+0.9	+1.5 (+1.3)	+1.2	+ 0.6
China	+7.4	+6.9	+6.7	+6.8 (+6.7)	+6.4	+ 1.8

2. The Bank of England announced a ¼% rise in interest rate on November 2nd, while the US Federal Reserve is to start reducing its balance sheet by not re-investing the proceeds of maturing bonds, and is expected to increase rates again in December. The European Central Bank is to halve its level of monthly bond purchases to €30bn from January 2018, with no specified end-date to the programme.

3. On September 22nd, in a speech in Florence, Theresa May set out more details of the UK's approach to the Brexit negotiations, but discordant voices within her Cabinet, and a troubled Conservative Party conference, have created renewed uncertainty about her tenure as Prime Minister, heightened by two Cabinet resignations early in November.

4. In the German Federal elections on September 24th, Angela Merkel won a fourth term as Chancellor, but her CDU party's share of the vote declined sharply, and the extremist AfD party won 13% of the votes. She must now seek a coalition with the Greens and the FDP, after the SPD withdrew as a coalition partner. Tensions in Spain increased after the call for independence from Catalonia; Madrid dissolved the regional parliament and assumed direct rule of the region pending a December election. In Japan, Prime Minister Abe

called a snap election for October 22nd in which he gained an important two-thirds majority in the Lower House.

5. Relations between North Korea and the United States deteriorated after North Korea carried out several missile tests, and President Trump responded with bellicose statements. Domestically, Trump has provoked more controversy with his equivocal comments after the rallies in Charlottesville, and disbanded two business advisory councils when members began to resign in protest at his remarks. Late in September, the Republicans published a tax reform plan, including reductions in corporate tax rates, which will now be debated in Congress.

Markets

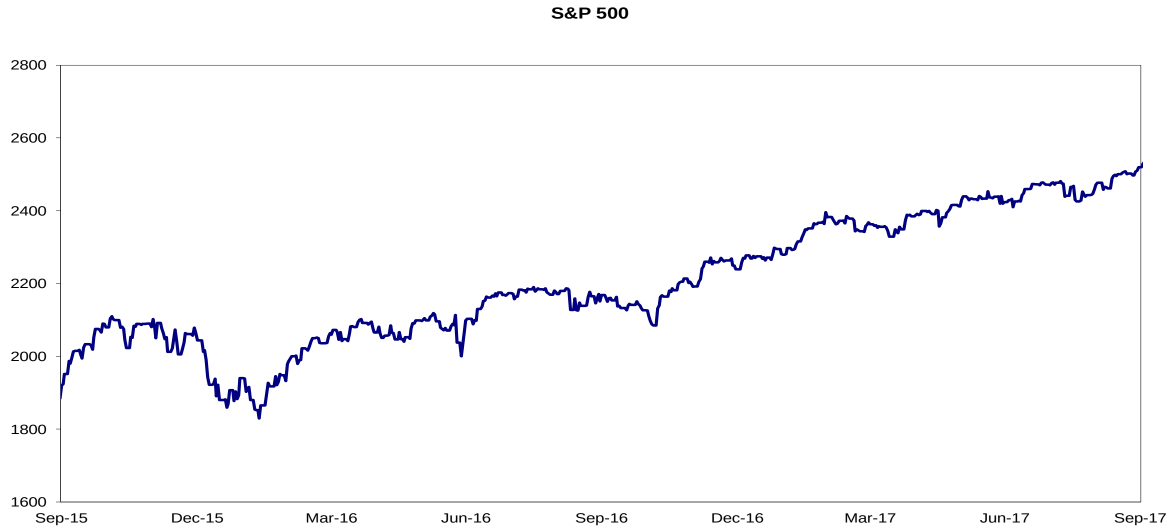
Equities

6. For the second successive quarter, equity markets were little changed. The UK market continues to deliver a return significantly below that of overseas equity markets, while Continental Europe has been by far the strongest region during the past year.

	Capital return (in £, %) to 30.9.17		
Weight %	Region	**3 months**	**12 months**
100.0	FTSE All-World Index	**+1.3**	**+12.7**
54.2	FTSE All-World North America	+0.9	+12.6
8.3	FTSE All-World Japan	+0.1	+9.3
12.2	FTSE All-World Asia Pacific ex Japan	+0.7	+12.3
16.4	FTSE All-World Europe (ex-UK)	+3.6	+18.9
6.2	FTSE All-World UK	+0.8	+6.9
9.6	FTSE All-World Emerging Markets	+3.3	+13.2

[Source: FTSE All-World Review, September 2017]

The US stockmarket has continued to push into record territory, helped by the strength of the big technology stocks - Facebook, Apple, Netflix and Google.



7. The rise in the price of oil, and the improving outlook for global economic growth boosted the Oil & Gas and Basic Materials sectors, while most other sectors showed little change over the quarter.

	Capital return (in £, %) to 30.9.17		
Weight %	**Industry Group**	**3 months**	**12 months**
13.0	Technology	+4.3	+22.3
22.9	Financials	+1.6	+20.4
4.9	Basic Materials	+6.2	+20.3
13.0	Industrials	+2.3	+17.0
100.0	**FTSE All-World**	**+1.3**	**+12.7**
13.0	Consumer Goods	-0.9	+7.7
10.5	Health Care	-1.0	+6.8
10.2	Consumer Services	-2.2	+6.5
3.2	Utilities	-0.2	+4.5
6.2	Oil & Gas	+5.2	+1.5
3.1	Telecommunications	-0.7	-3.6

[Source: FTSE All-World Review, September 2017]

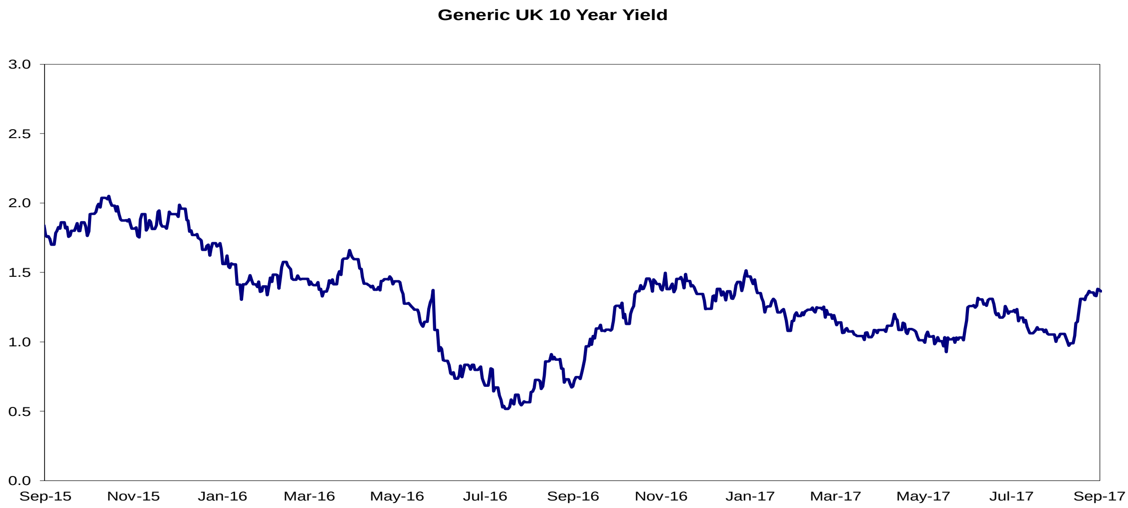
8. The mid- and small-cap sectors of the UK market have out-performed the FTSE 100 over the past 3 and 12 months.

(Capital only%, to 30.9.17)	3 months	12 months
FTSE 100	+ 0.8	+ 6.9
FTSE 250	+ 2.8	+11.2
FTSE Small Cap	+ 2.3	+14.8
FTSE All-Share	+ 1.2	+ 7.8

Bonds

9. As was the case in the second quarter, there was very little net change in the yields on medium-term government bonds in the major markets.

The 10-year gilt has now traded at a yield below 1.5% since the spring of 2016 (see graph below)



10-year government bond yields (%)					
	Dec ’14	Dec 2015	Dec 2016	June 2017	Sept 2017
US	2.17	2.27	2.46	2.28	2.32
UK	1.76	1.96	1.24	1.33	1.41
Germany	0.54	0.63	0.11	0.47	0.47
Japan	0.33	0.27	0.04	0.09	0.05

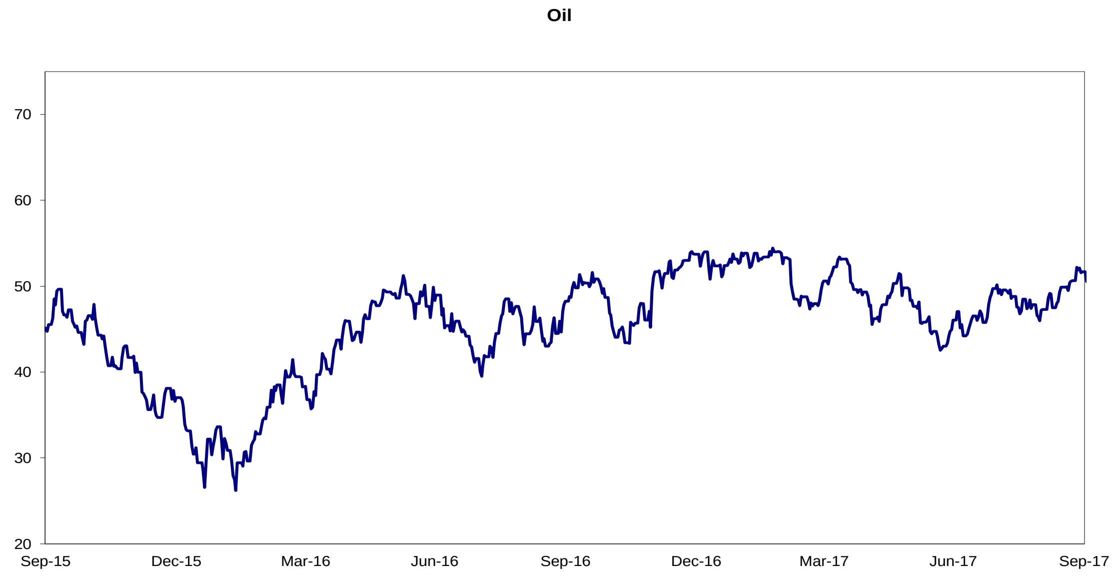
Currencies

10. The dollar and the yen were the weaker currencies during the quarter, while the pound kept pace with the euro. At one stage the pound reached $1.36 – its highest level against the dollar since the EU referendum – but in early October it retreated to $1.31 (see graph below)

				£ move (%)	
	30.9.16	**30.6.17**	**30.9.17**	**3m**	**12m**
$ per £	1.299	1.299	1.342	+ 3.3	+ 3.3
€ per £	1.156	1.139	1.135	- 0.4	- 1.9
Y per £	131.5	146.0	151.0	+ 3.4	+14.8

Commodities

11. The price of Brent crude rose by over 15% during the quarter to reach $57 per barrel, its highest level for two years. This has been the result of a number of factors – the maintenance of the production curbs announced by OPEC countries and Russia in November 2016; the threat by President Erdogan of Turkey's to turn off an Iraqi pipeline, and the interruptions to refining operations in Texas caused by Hurricane Irma. Events in Iraq and Saudi Arabia caused the price to reach $64 per barrel in early November.



Property

12. Returns on UK Property during the past year reflect the improvement in sentiment, and overseas demand for UK trophy assets, since the EU Referendum. Industrials have continued to be the strongest sector by a wide margin.

	3-month (%)	12-month
All Property	**+ 2.7**	**+10.4**
Retail	**+ 1.9**	**+ 7.6**
Office	**+ 2.0**	**+ 8.1**
Industrial	**+ 4.8**	**+18.6**

[MSCI UK Monthly Index of total returns, Sept 2017]

Outlook

13. Equity markets have continued steadily upwards, reaching all-time highs in many markets, despite geo-political concerns surrounding developments in North Korea and the Middle East and the rising oil price. The move in UK interest rates, the imminent rise in US rates, and the tapering of quantitative easing in US and Europe all appear likely reduce the flows of liquidity into markets generally.

14. By the same token, government bond market yields are likely to rise in response to higher short-term rates, unless they become ‘safe havens’ in the event of political crisis, or if global economic growth begins to slow down. In either of these situations, equities can be expected to weaken significantly.

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[All graphs supplied by Legal & General Investment Management]