DORSET COUNTY PENSION FUND

Quarterly Report 31 December 2017

YOUR PORTFOLIO

Fund performance objective

The fund objective is to outperform the benchmark by 0.5% per annum net of the standard management fees.

Fund asset allocation and benchmark ranges

Fund and benchmark index	Fund allocation (%)
RLPPC Over Five Year Corporate Bond Fund Benchmark: iBoxx Sterling Non-Gilt Over 5 Year Index.	100.0

Portfolio value

	Portfolio total (£m)
31 December 2017	**206.74**
30 September 2017	318.56
Change over quarter	(111.82)
Net cash inflow (outflow)	(120.00)

EXECUTIVE SUMMARY

Performance

- The Fund gave a gross return of 3.05% over the quarter, compared with a benchmark return of 2.41%.
- Credit markets were generally resilient in the fourth quarter, against a backdrop of monetary policy tightening, as investor appetite for risk remained steady and plans for an overhaul of the US tax system moved ahead. The US economy remained strong and growth improved in Europe, while UK data continued to be broadly positive, despite Brexit uncertainty.
- The most prominent sources of outperformance were the Fund's overweight allocation to financials, particularly to subordinated debt, and the stock selection within secured and structured debt.

The economy and bond markets

- A positive global outlook continued to bolster investor sentiment, but political concerns were evident in some markets. While Brexit talks can now move ahead to the next stage, the UK government was defeated in a key vote that means any agreement to leave the bloc must be approved by Parliament. In Germany, talks on forming a new coalition government broke down, potentially leaving Chancellor Angela Merkel to form a minority administration or fight a snap election. Spain's central government and the regional administration in Catalonia clashed in October over a referendum on Catalan autonomy; in December, three pro-independence parties won a majority of seats in Catalonia's parliament.
- At its December meeting, the US Federal Reserve (Fed) raised its key policy rate for a third time in 2017 and continued to project three further increases in 2018. The European Central Bank (ECB) left interest rates unchanged, but in October announced a further reduction in the pace of its monthly asset purchases, effective as of January 2018. The Bank of England (BoE) raised its key rate in November for the first time in a decade, reversing the emergency cut that followed the Brexit referendum, and policy makers endorsed an outlook that assumes two more increases by 2020. UK government bond yields fell sharply near the end of the quarter, while most European markets registered small rises.
- Sterling investment grade credit underperformed UK conventional and index linked government bonds. Gilt yields fell and the average sterling investment grade credit spread narrowed by 1 basis point (bp) to 104bps.

Investment outlook

- Our base case is that global growth remains close to recent rates, but below its pre-crisis average.
- We expect UK growth to be supported by falling inflation through 2018, although uncertainty about Brexit will act as a constraint.
- We expect a rate rise by the BoE in the third quarter of 2018 and three increases from the Fed in the coming year.

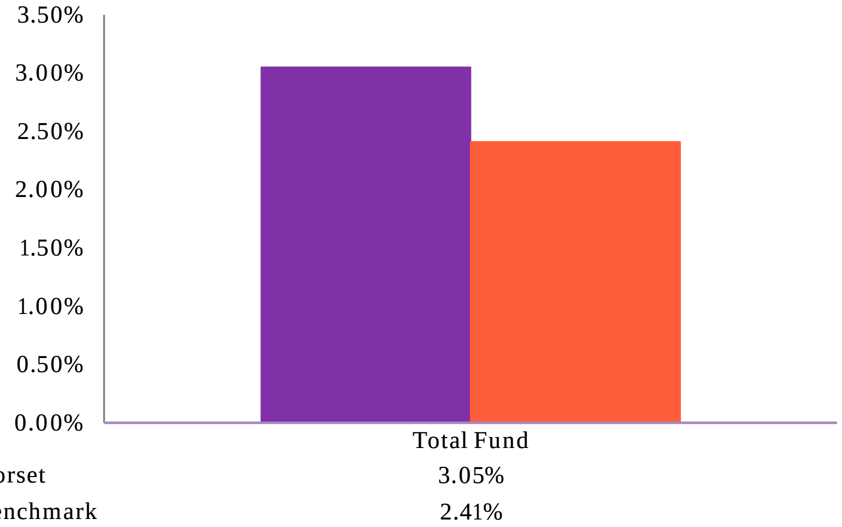
FUND PERFORMANCE

The table below shows the gross performance of your portfolio and the benchmark for the periods ending 31 December 2017.

Performance

	Fund (%)	Benchmark (%)	Relative (%)
Q4 2017	**3.05**	**2.41**	**0.64**
Rolling 12 months	7.90	5.47	2.43
3 years p.a.	7.12	6.20	0.92
5 years p.a.	8.03	6.79	1.24
Since inception 02.07.07 p.a.	9.21	9.20	0.01

Quarterly performance



RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Asset split

	Fund (%)	Benchmark[1] (%)
Conventional credit bonds[2]	99.8	98.8
Index linked credit bonds	0.0	0.0
Sterling conventional gilts	0.0	0.0
Sterling index linked gilts	0.0	0.0
Foreign conventional sovereign	0.2	1.2
Foreign index linked sovereign	0.0	0.0
Derivatives	0.0	0.0

Fund data

	Fund	Benchmark[1]
Duration	10.4 years	10.5 years
Gross redemption yield[3]	2.95%	2.50%
No. of stocks	226	686
Fund size	£290.1m	-

Launch date: 02.07.2007

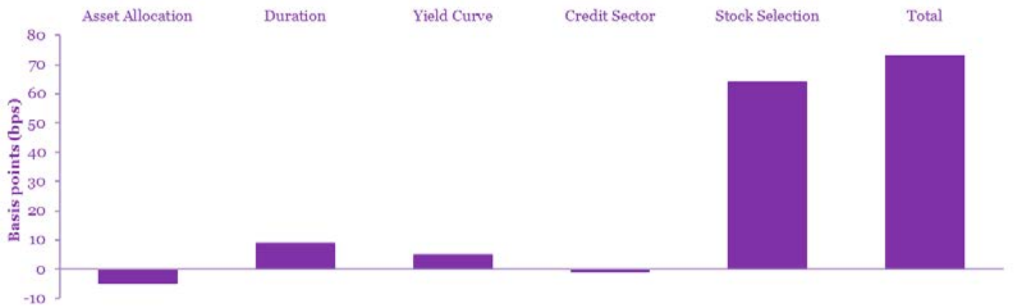
[1] Benchmark: iBoxx Sterling Non-Gilt Over 5 Year Index.

[2] Conventional credit bond allocation includes exposure to non-sterling credit bonds and CDs, where applicable.

[3] The gross redemption yield is calculated on a weighted average basis.

Figures in relation to the asset spilt table exclude the impact of cash where held.

Performance attribution for quarter 4 2017

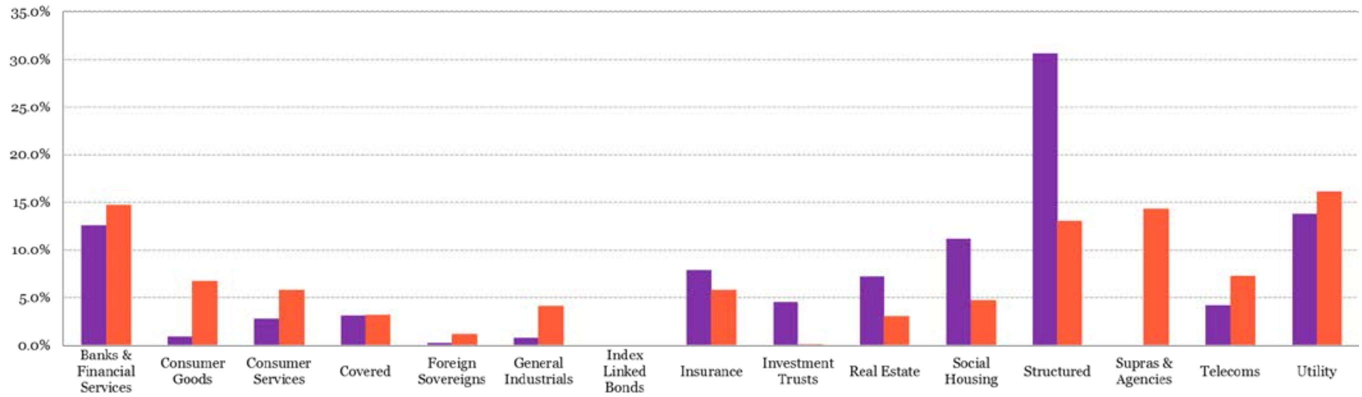


Source: *RLAM and UBS Delta. The above performance attribution is an estimate. Please note that the attribution chart does not include residual effect returns.*

RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Sector breakdown



	Banks & Financial Services	Consumer Goods	Consumer Services	Covered	Foreign Sovereigns	General Industrials	Index Linked Bonds	Insurance	Investment Trusts	Real Estate	Social Housing	Structured	Supras & Agencies	Telecoms	Utility
PPLCP	12.6%	0.9%	2.8%	3.1%	0.2%	0.8%	0.0%	7.9%	4.5%	7.2%	11.2%	30.6%	0.0%	4.2%	13.8%
Benchmark	14.7%	6.8%	5.8%	3.1%	1.2%	4.1%	0.0%	5.8%	0.1%	3.0%	4.7%	13.0%	14.3%	7.2%	16.1%

Source: *RLAM. Figures in relation to your portfolio exclude the impact of cash held, although they do include the impact of CDs if held within your portfolio.*

What we thought	What we did	What happened	Effect on portfolio
We expected that corporate bonds would outperform supranational debt.	The Fund sold its small exposures to supranational debt, increasing the significant overweight position in corporate bonds. The Fund's holding in gilts was also sold late in the quarter.	Supranational debt underperformed the broader sterling credit market over the quarter, and the year as a whole. Positive risk sentiment and demand for yield continued to spur demand for corporate bonds. Conversely, gilts outperformed over the fourth quarter.	The Fund's substantial underweight position in supranationals had a small positive impact upon relative performance. The small exposure to gilts did not have a material impact on Fund returns.
We continued to see value in financials (banks and insurers), and to favour a combination of covered bonds and subordinated bank debt over senior bonds.	The allocation to financials ended the quarter in line with that of the benchmark index. Within this allocation, we moderated the underweight exposure to senior unsecured debt, maintaining the above-benchmark exposures to subordinated debt. Exposure to covered bonds was reduced in the quarter and brought into line with the benchmark.	The noticeable sector trend of 2017 continued in the final quarter of the year with financial sectors performing strongly, led by subordinated debt, amid ongoing improvement of capital positions to meet tougher regulatory requirements, and investors' continuing demand for higher yielding assets. Covered bonds underperformed the broader market.	The preference for subordinated financial debt was a strong driver of performance in the fourth quarter and for 2017 as a whole. The exposure to covered bonds had a small negative effect on relative performance.

ROYAL LONDON

RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

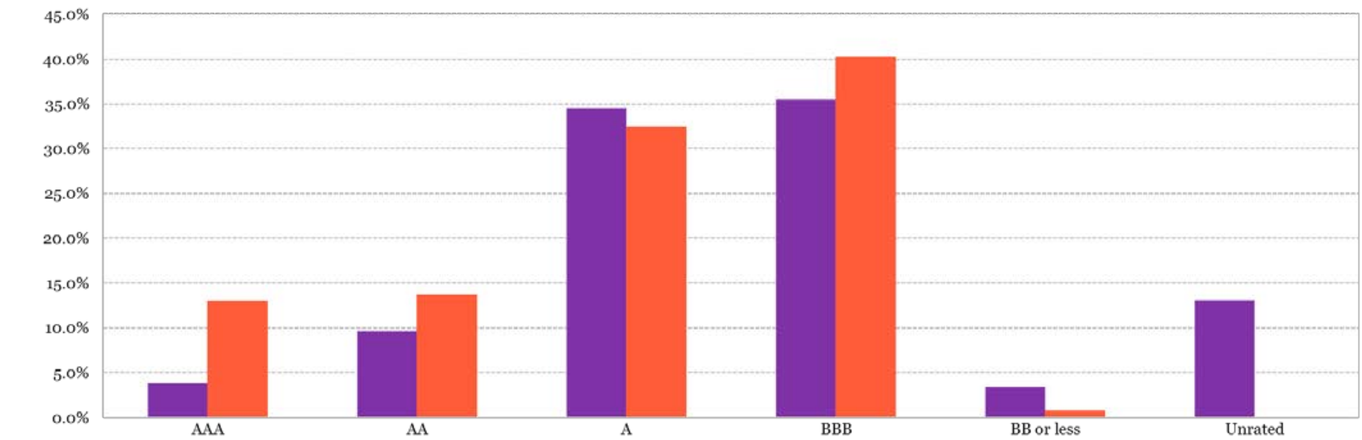
Sector breakdown continued

What we thought	What we did	What happened	Effect on portfolio
We thought that high-profile, consumer-orientated bonds and industrials were unattractively priced, relative to other sectors.	We increased the underweight allocation to industrial and consumer sectors.	Having lagged the broader market for much of the year, consumer sectors continued to mostly underperform, as consumer spending began to reflect the impact of inflation outpacing wage growth. Conversely, industrials performed relatively well.	The low weightings in consumer and industrial sectors did not have a significant impact upon relative performance.
We continued to believe that secured bonds were undervalued relative to unsecured debt.	We increased the Fund's significant overweight positions in sectors that benefit from enhanced security, e.g. asset backed securities (ABS), social housing and investment trusts.	Secured and structured sectors, which typically comprise longer dated bonds and span a wide spectrum of industries, performed in line with the broader credit market.	The Fund benefited from stock selection within secured and structured debt over the quarter and the entire year.

RLPPC OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Rating breakdown



	AAA	AA	A	BBB	BB or less	Unrated
PPLCP	3.8%	9.6%	34.6%	35.5%	3.4%	13.1%
Benchmark	13.0%	13.7%	32.4%	40.2%	0.7%	0.0%

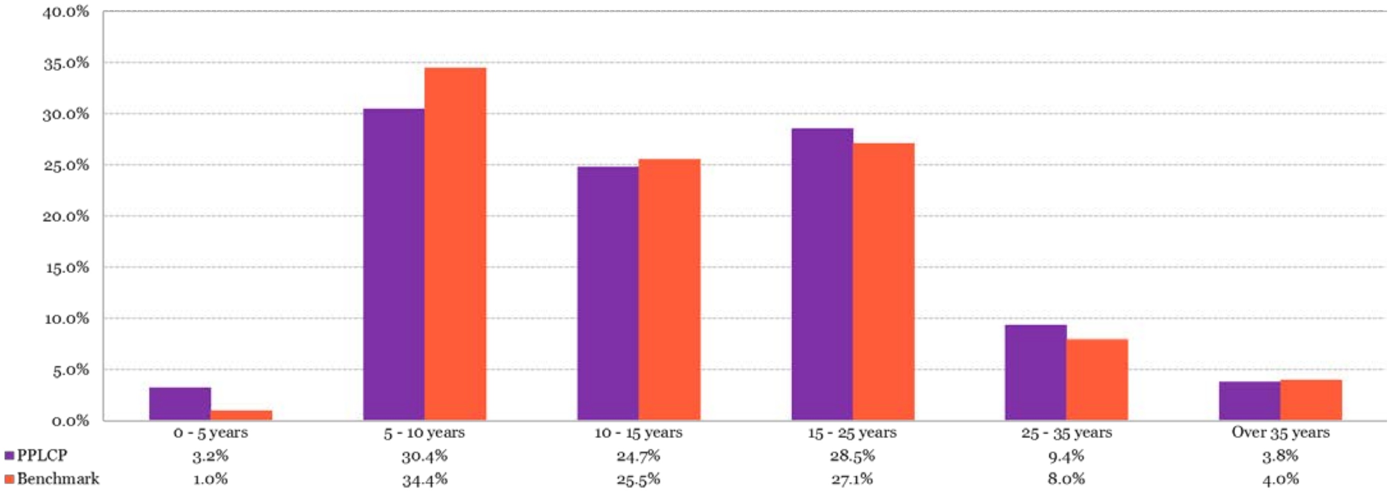
Source: *RLAM. Figures in relation to your portfolio exclude the impact of cash held, although they do include the impact of CDs if held within your portfolio.*

What we thought	What we did	What happened	Effect on portfolio
We believed lower rated credit bonds offered better value than AAA / AA rated securities.	The bias towards lower rated bonds was maintained over the quarter, with the magnitude of the position increased slightly.	Lower rated investment grade issues outperformed higher rated counterparts over the quarter and the year as a whole, helped by steady investor appetite for risk.	The bias towards lower rated debt was beneficial for relative performance over the fourth quarter and the entire year.
Credit ratings, while useful, are not a complete assessment of creditworthiness and value.	We maintained exposure to bonds rated below investment grade where we believed they were consistent with the overall objective of the Fund. In part, this exposure reflected the Fund's holding in the Royal London Sterling Extra Yield Fund, which was sold late in the quarter. Exposure to unrated bonds, which predominantly have investment grade risk characteristics and are in many instances secured, was broadly unchanged.	High yield bonds underperformed investment grade credit in the quarter, hurt by investor outflows and negative news from the media and technology sectors in November. For all of 2017, however, high yield outperformed, reflecting positive sentiment that supported riskier assets. The Royal London Sterling Extra Yield Bond Fund posted a gross return of 2.65% over the entire quarter, compared with the 1.83% return for the broader investment grade sterling credit market.	Exposure to unrated bonds and to the Royal London Sterling Extra Yield Fund had a positive impact upon performance.

RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Maturity profile



Source: *RLAM. Figures in relation to your portfolio exclude the impact of cash held, although they do include the impact of CDs if held within your portfolio.*

What we thought	What we did	What happened	Effect on portfolio
We expected a gradual increase in UK government bond yields.	The Fund's short duration versus the benchmark was broadly maintained over the quarter.	Despite the rise in base rates by the Bank of England in November, reversing the emergency cut that followed the Brexit referendum result, government bond yields fell slightly over the quarter as a whole, as uncertainty over Brexit prevailed. Yields were volatile over the year, but ended 2017 only marginally lower.	The short duration position did not have a significant impact upon relative performance.

RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Ten largest holdings

	Weighting (%)
Prudential Plc 5.7% VRN 2063	1.2
HSBC Bank 5.375% 2033	1.2
Finance for Residential Social Housing 1997 8.368% 2058	1.2
Bank Of America 7% 2028	1.1
Innogy Finance BV 6.125% 2039	1.1
Lloyds Bank Plc 6% 2029	1.1
Enel Finance 5.75% 2040	1.0
Equity Release 5.7% 2031	1.0
Thames Water Utilities Finance 7.738% 2058	1.0
Exchequer Partnership 5.396% 2036	1.0
Total	**10.9**

Source: *RLAM. Figures in the table above exclude derivatives where held.*

RLPPC UK OVER 5 YEAR CORPORATE BOND FUND

Quarter 4 2017

Fund activity

- The Fund's exposures to gilts and supranationals were sold late in the quarter with proceeds reinvested into credit bonds, predominantly into secured sectors and structured bonds; the bias within the Fund to these sectors was raised by around 9% over the quarter. Exposure to covered bonds was slightly reduced, ending the quarter in line with that of the benchmark.
- The Fund's exposure to the **Royal London Sterling Extra Yield Bond Fund** was sold late in the quarter. The Royal London Sterling Extra Yield Bond Fund returned 2.65% gross over the entire quarter, compared to the 1.83% return posted by the broader sterling investment grade credit market.
- Sterling credit issuance was strong over the quarter as a whole, albeit tailing off into the end of the December, bringing the level of issuance for 2017 as a whole above that of the previous year.
- New issue purchases in structured and secured sectors included the first bond issued by the Student Loans Company (**Income Contingent Student Loans**), where the underlying loan repayments of this A rated structured bond are contingent upon the borrower earning above a threshold amount. The deal had been introduced in February 2017, but was postponed on account of the snap election. The Fund bought bonds from the A1 (floating rate) and A2 (fixed rate) tranches. Within social housing, new issues were purchased from London-based **Catalyst Housing**, partly funded by selling exposure to brewer **InBev**; **Housing and Care 21**, which focuses on older people; and **WM Housing Group**, a West Midlands-based housing association. The Fund also bought new 14-year bonds from real estate investment trust **Tritax Big Box**, which leases logistics sites to tenants including Amazon and DHL, and subsequently sold the debt to help manage cashflows. A 30-year issue from real estate investment manager **Eskmuir Group** also was purchased, after the Fund's existing holding was called at an attractive premium to the prevailing market price.
- Elsewhere in new issues, the Fund took part in the first debt issue by AAA rated **University of Oxford**, which raised £750m through its 100-year bond. In telecommunications, the Fund bought senior unsecured bonds of **Verizon**.
- In the secondary market, the Fund sold its holdings of supranational debt, comprised of exposures to Singapore state investor **Temasek** and **SNCF Reseau**, the infrastructure division of France's national railway company.
- The Fund sold a variety of exposures late in the quarter to help manage cashflows and fund new issuance activity. Within secured and structured sectors, the Fund sold or reduced allocations to **Gatwick** and **Dignity Finance**, as well as real estate companies **Lend Lease** and **Vicinity Centres** and social housing associations **Peabody Capital**, **Sanctuary** and **London & Quadrant**. In financials, the Fund sold exposures including **Swiss Reinsurance**, **Metropolitan Life** and **Coventry Building Society**, and also covered bonds of **Royal Bank of Scotland**, **National Australia Bank** and **Nationwide Building Society**. Other exposures sold by the Fund included retailer **John Lewis**, packaging company **DS Smith** and transportation companies **Stagecoach** and **East Japan Railway**.
- Continuing a trend of 2017, with issuers taking advantage of persistently low yields to reduce debt costs, the Fund participated in a tender of its holding in 2038 maturity bonds from **Pfizer** at an attractive spread premium, in exchange for longer dated 2043 debt.

Key views in your portfolio

- A significant underweight in supranational bonds, as we expect corporate bonds to outperform over the medium term.
- Duration shorter than that of the benchmark, as we expect underlying gilt yields to gradually trend higher over 2018.
- A bias towards asset backed securities, an area that we believe still offers the best risk/return characteristics.
- An overweight position in subordinated financial debt, where we believe yields are attractive.

FURTHER INFORMATION

MARKET COMMENTARIES & INVESTMENT OUTLOOK

- Please click on link for further information.

CORPORATE GOVERNANCE & COMPLIANCE

- Please click on link for further information.

GLOSSARY

- Please click on link for a glossary on terms.

RLAM TEAM

Your fund managers

Jonathan Platt
Head of Fixed Income

Shalin Shah
Credit Fund Manager

Paola Binns
Senior Fund Manager

Your dedicated contact

Rob Nicholson
Client Relationship Director

T: 020 3272 5281
F: 020 7506 6784
E: robert.nicholson@rlam.co.uk

In Rob's absence, please feel free to contact any of the Client Relationship team members listed below or email: ClientRelationships@rlam.co.uk.

Lucy Bramwell	T: 020 3272 5279	E: lucy.bramwell@rlam.co.uk
Fraser Chisholm	T: 020 3272 5278	E: fraser.chisholm@rlam.co.uk
Mark Elbourne	T: 020 3272 5282	E: mark.elbourne@rlam.co.uk
Daniel Norsa Scott	T: 020 3272 5280	E: daniel.norsascott@rlam.co.uk
Andrew Cunningham	T: 020 3272 5468	E: andrew.cunningham@rlam.co.uk
John Matthews	T: 020 3272 5423	E: john.matthews@rlam.co.uk

Portfolio Valuation

As at 31 December 2017

Dorset County Pension Fund

	Holding	Identifier	Asset Description	Market Price (Bid £)	Book Cost Capital (£)	Market Cap. Value (£)	Accrued Inc. Value (£)	Market Value (£)	Days Accrued	Market Value %
Funds Held										
	84,889,523	GB00B1ZB3X88	RLPPC Over 5 Year Corp Bond Pen Fd	2.43536	107,075,379.68	206,736,547.72	0.00	206,736,547.72	0	100.0
				Funds Held total	**107,075,379.68**	**206,736,547.72**	**0.00**	**206,736,547.72**		**100.0**
				Grand total	**107,075,379.68**	**206,736,547.72**	**0.00**	**206,736,547.72**		**100.0**

Trading Statement

For period 01 October 2017 to 31 December 2017

Dorset County Pension Fund

	Trade Date	Transaction Type	Nominal	Security	Price (£)	Book Cost (£)
Acquisitions						
Funds Held						
	05 Oct 2017	Acquisition Rebate	102,217.04	RLPPC Over 5 Year Corp Bond Pen Fd	2.39	244,160.73
					Funds Held total	**244,160.73**
					Acquisitions total	**244,160.73**

Trading Statement

For period 01 October 2017 to 31 December 2017

Dorset County Pension Fund

	Trade Date	Transaction Type	Nominal	Security	Price (£)	Book Cost (£)	Proceeds (£)
Disposals							
Funds Held							
	27 Nov 2017	Disposal	41,648,272.01	RLPPC Over 5 Year Corp Bond Pen Fd	2.40	52,533,038.28	100,000,000.00
	13 Dec 2017	Disposal	8,266,307.36	RLPPC Over 5 Year Corp Bond Pen Fd	2.42	10,426,704.88	20,000,000.00
					Funds Held total	**62,959,743.16**	**120,000,000.00**
					Disposals total	**62,959,743.16**	**120,000,000.00**