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London Borough of Tower Hamlets  
Quarter Ending 30 September 2014

**Client Relationship Manager**

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Investment  
Management Review

# London Borough of Tower Hamlets

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## *Table of Contents*

*Quarter Ending 30 September 2014*

<b>Performance</b>	3
<b>Change in Market Value</b>	5
<b>Investment Review</b>	6
<b>Profile Summary</b>	7
<b>Attribution</b>	9
<b>Process Review</b>	11

# London Borough of Tower Hamlets

## Performance Gross of Management, Operating, Incentive Fees in GBP

Periods Ending 30 September 2014

Investment	Month	Quarter	YTD	Annualised			*Since Inception	Market Value (000)
				1 Year	3 Year	5 Year		
Global Equity Separately Managed (GBP) (29/04/2005)	-1.10 %	0.38 %	5.24 %	11.06 %	14.77 %	9.44 %	9.27 %	268,708
London Borough of TH Custom Benchmark	-0.88	1.59	4.14	8.66	14.92	9.22	9.17	
Value Added	-0.22	-1.21	1.10	2.40	-0.15	0.22	0.10	

\* Periods of less than a year are not annualised

**Note:**

The London Borough Custom Benchmark is comprised of 30% FTSE World North America, 30% FTSE Developed Europe ex-UK Index, 17% FTSE Japan Index, 10% FTSE All-Share, 8.5% FTSE Developed Asia Pacific ex-Japan Index (ex Korea effective 21sep09), 4.5% MSCI Emerging Markets Index.

# London Borough of Tower Hamlets

## Performance Net of Fees and Expenses in GBP

Periods Ending 30 September 2014

Investment	Month	Quarter	YTD	Annualised			*Since Inception	Market Value (000)
				1 Year	3 Year	5 Year		
<b>Global Equity Separately Managed (GBP) (29/04/2005)</b>	-1.12 %	0.32 %	5.06 %	10.82 %	14.40 %	9.03 %	8.81 %	268,708
<i>London Borough of TH Custom Benchmark</i>	-0.88	1.59	4.14	8.66	14.92	9.22	9.17	
Value Added	-0.24	-1.27	0.92	2.16	-0.52	-0.19	-0.36	

\* Periods of less than a year are not annualised

**Note:**

The London Borough Custom Benchmark is comprised of 30% FTSE World North America, 30% FTSE Developed Europe ex-UK Index, 17% FTSE Japan Index, 10% FTSE All-Share, 8.5% FTSE Developed Asia Pacific ex-Japan Index (ex Korea effective 21sep09), 4.5% MSCI Emerging Markets Index.

# London Borough of Tower Hamlets

## *Change in Market Value, Account Detail in GBP*

*QTD Ending 30 September 2014*

<b>Fund</b>	<b>Market Value 30/06/2014</b>	<b>Cash Flows</b>	<b>Gains/ Losses</b>	<b>Market Value 30/09/2014</b>
London Borough of Tower Hamlets Pension Fund	267,721,761	-28,955	1,015,638	268,708,444
<b>Total</b>	<b>267,721,761</b>	<b>-28,955</b>	<b>1,015,638</b>	<b>268,708,444</b>

*If you are an investor in a GMO fund who receives statements directly from the relevant Fund's transfer agent or administrator, we urge you to compare those statements with your GMO statements.*

### Transaction Details

<b>Date</b>	<b>Transaction</b>	<b>Gross Amount</b>
<b>London Borough of Tower Hamlets Pension Fund in GBP</b>		
18/08/2014	Redemption	-29,088.03
21/08/2014	Purchase	133.22

# London Borough of Tower Hamlets

## *Global Equity Strategy - Investment Review*

*Quarter Ending 30 September 2014*

### **Global Equity Strategy**

**Product Manager:** Kim Mayer

#### **Overview:**

- The Strategy seeks to deliver high total return by investing in equities or groups of equities that the GMO Global Equity team believes will provide higher returns than the benchmark.
- The Strategy uses multi-year forecasts of returns among asset classes to build a portfolio that typically provides exposure to global equity markets.

Global equities posted generally negative results during the third quarter, as growing concerns about geopolitical instability combined with less certainty about future sources of global stimulus to shake the bullish complacency of the first half of the year. The key elements of geopolitical risk include the evolution of ISIS within the Middle East and the Russia/Ukraine conflict, as well as the response of the West to these events. On the Central Bank policy front, we are at a potential inflection point within the U.S. in the present transition from Fed stimulus to neutrality. The MSCI ACWI index fell 2.3% for the quarter. The U.S. market was the only broad regional market to post positive returns for the quarter, with the S&P 500 registering modest gains of 1.1%. In developed international markets, MSCI EAFE was down 5.9% for the quarter as Europe was hard hit. MSCI Europe declined 7.0% over the quarter. Japan fared a bit better, but was still in negative territory with the MSCI Japan index shedding 2.3% for the quarter. Emerging markets also posted losses. The MSCI Emerging index fell 3.5% for the third quarter.

Weak returns for most equity markets globally during the third quarter generally resulted in modest gains for GMO's assessment of equity market opportunities with the exception of the U.S. market. In the U.S., we favor high quality stocks from a group level valuation perspective. Quality stocks essentially matched the returns of the S&P for the quarter. Our forecast for U.S. high quality stocks at the end of the quarter was unchanged at 2.2%. Among international developed equities we continue to favor value stocks, particularly within Europe. Our forecast for European value stocks (excluding financials) at the end of the third quarter was 1.8%. We also continue to favor emerging market equities. Our emerging market equities forecast increased to 3.7% at the end of the quarter, as compared to 3.6% at the end of the second quarter.

During the quarter, our allocations within the portfolio changed incrementally. We maintain key exposures to U.S. quality equities, European value stocks, and emerging market equities.

# London Borough of Tower Hamlets

## Global Equity Strategy - Profile Summary

As of 30 September 2014

Top Ten Holdings <sup>2</sup>		Risk Profile		Group Exposures <sup>4</sup>	
		Since 30/04/2005 <sup>3</sup>			
		Portfolio	Benchmark <sup>1</sup>		
Amazon.com Inc.	3.8%	Alpha	-.24	US Quality	28.4%
Philip Morris International Inc.	3.3%	Beta	.98	US Opportunistic Value	10.1%
Total S.A.	2.9%	R-Squared	.98	Europe Value	39.6%
Royal Dutch Shell PLC	2.9%	Sharpe Ratio	.50	Japan	10.6%
Express Scripts Holding Co	2.7%			Other Int'l Opportunistic Value	0.6%
Microsoft Corp.	1.9%			Emerging Markets	9.1%
Japan Tobacco Inc.	1.8%			Cash & Cash Equiv.	1.6%
Oracle Corp.	1.8%				
International Business Machines Corp.	1.7%				
BP PLC	1.7%				
<b>Total</b>	<b>24.5%</b>				

Characteristics		
	Portfolio	Benchmark <sup>1</sup>
Price/Earnings - Hist 1 Yr Wtd Median	15.6x	18.2x
Price/Cash Flow - Hist 1 Yr Wtd Median	8.9x	12.0x
Price/Book - Hist 1 Yr Wtd Avg	1.6x	1.8x
Return on Equity - Hist 1 Yr Med	13.4%	12.4%
Market Cap - Weighted Median -Bil	32.5 GBP	19.2 GBP
Number of Equity Holdings	721	3297
Dividend Yield - Hist 1 Yr Wtd Avg	3.1%	2.6%

<sup>1</sup> London Borough of TH Custom Benchmark

<sup>2</sup> Portfolio holdings are a percent of equity. They are subject to change and should not be considered a recommendation to buy individual securities.

<sup>3</sup> Alpha is a measure of risk-adjusted return; Beta is a measure of a portfolio's sensitivity to the market; R-Squared is a measure of how well a portfolio tracks the market; Sharpe ratio is the return over the risk free rate per unit of risk. Risk profile data is net.

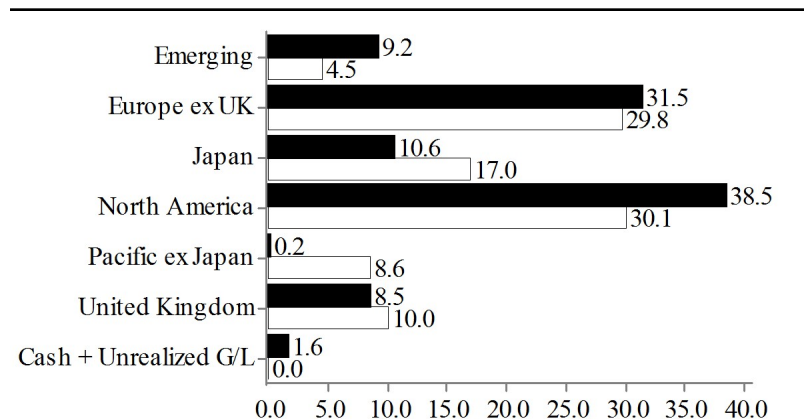
<sup>4</sup> The groups indicated above represent exposures determined pursuant to proprietary methodologies and are subject to change over time.

# London Borough of Tower Hamlets

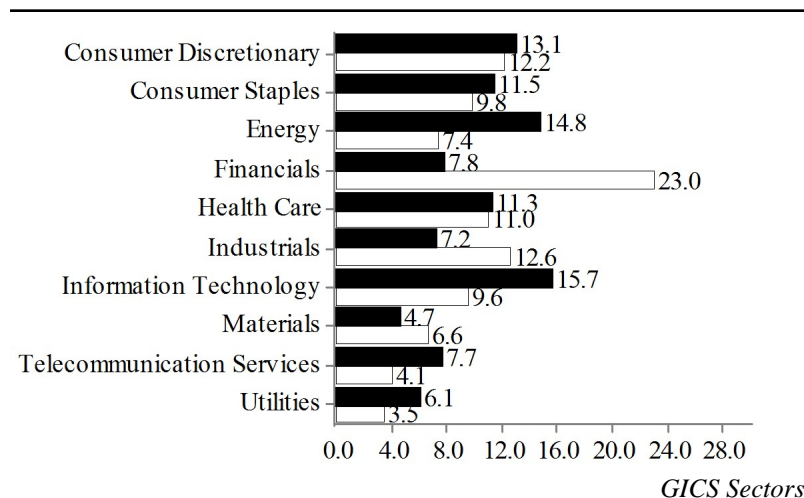
## Global Equity Strategy - Profile Summary

As of 30 September 2014

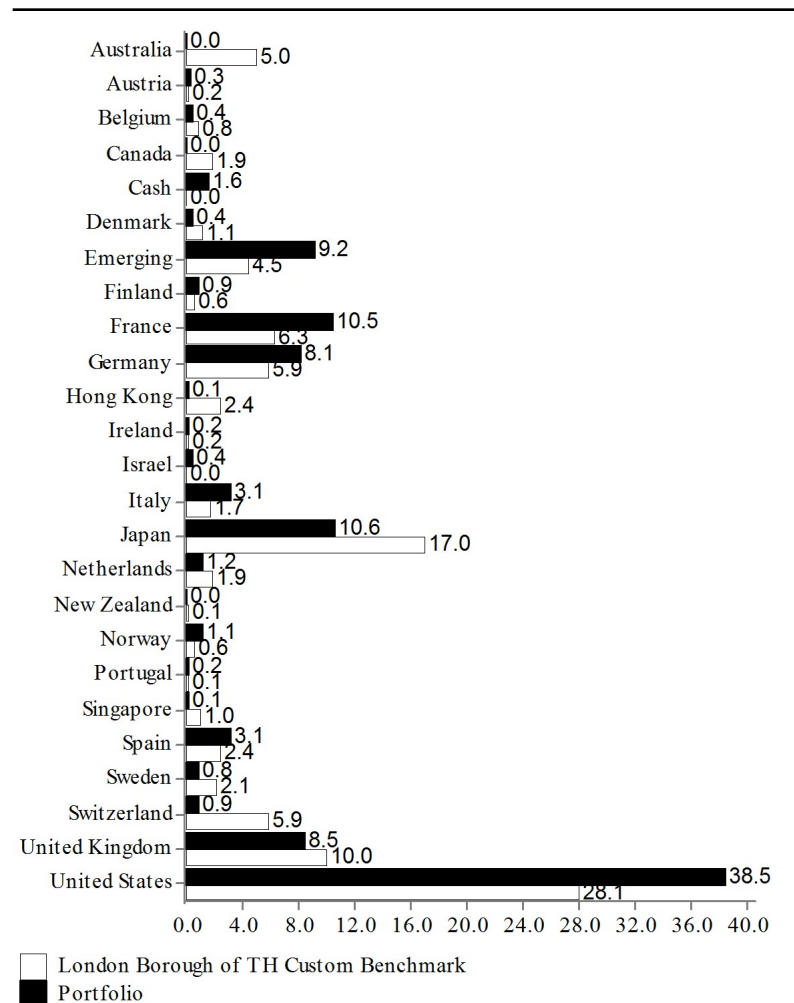
**Regional Weights**



**Sector Weights**



**Country Allocation**





# London Borough of Tower Hamlets

## Global Equity Strategy - Attribution Overview

Quarter Ending 30 September 2014

### Performance (%)

Net of Fees, USD (Rep Account)	-5.30
Gross of Fees, USD (Rep Account)	-5.05
MSCI World	-2.16
<b>Value Added</b>	<b>-2.89</b>

### GROUP ALLOCATION: -1.0%



### SECURITY SELECTION: -1.9%



### Major Performance Drivers

#### U.S. High Quality

*Characteristics:* Our position in U.S. high quality is comparatively multinational and carries less cyclical economic exposure compared to the U.S. market.

*Positioning:* U.S. high quality accounted for approximately 26% of our total portfolio weight during the quarter.

*Results:* Our position in U.S. high quality produced a positive allocation impact and a modestly positive selection impact during the quarter. High quality stocks outperformed the U.S. market during the period as U.S. investors favored Health Care and Information Technology over more cyclical sectors such as Energy and yield-sensitive sectors such as Utilities.

#### Emerging Markets

*Characteristics:* Our position in emerging markets is focused on undervalued segments within the market that have recently fallen out of favor with investors, highlighted by a position in Russia Energy.

*Positioning:* Emerging markets accounted for approximately 10% of our total portfolio weight during the quarter.

*Results:* Our emerging markets position produced negative allocation and selection impacts during the quarter, as the asset class underperformed global indices and our valuation-driven selections underperformed within the region. Leading country-sector detractors during the period included Russia Energy and Brazil Utilities, while China Telecommunication Services was the leading contributor.

The above information is based on a representative account in the Strategy selected because it has the fewest restrictions and best represents the implementation of the Strategy.

# London Borough of Tower Hamlets

## Global Equity Strategy - Attribution Overview

Quarter Ending 30 September 2014

### Major Performance Drivers (continued)

#### Japan

*Characteristics:* Our position in Japan is focused primarily on value stocks within the region selected by both quantitative and fundamental valuation approaches.

*Positioning:* Japan accounted for approximately 10% of our total portfolio weight during the quarter.

*Results:* Our Japan position produced a neutral allocation impact and a negative selection impact during the quarter. Japan performed in line with the global index, while our value oriented stock selections underperformed within the region. Sectors in which our selections delivered negative relative returns included Industrials and Consumer Staples.

#### European Value

*Characteristics:* Our position in European value carries a fair amount of exposure to some of the more cyclically-exposed segments of the market and is currently the largest group-level allocation in the strategy.

*Positioning:* European value accounted for approximately 41% of our total portfolio weight during the quarter.

*Results:* Our position in European value produced a negative allocation impact during the quarter, as European stocks trailed the broader market. This was further affected by negative selection impacts, as our valuation-focused positions underperformed. Selections within countries including the United Kingdom and Germany were the leading detractors from returns.

# London Borough of Tower Hamlets

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## *Global Equity Strategy - Process Review*

### **Overview**

The GMO Global Equity Strategy seeks to deliver high total return by investing in equities or groups of equities that the GMO Global Equity team believes will provide higher returns than the benchmark.

The Strategy uses multi-year forecasts of returns among asset classes to build a portfolio that typically provides exposure to global equity markets.

### **Methodology**

GMO's Global Equity team uses active investment management methods, which means that equities are bought and sold according to the team's evaluation of companies' published financial information and corporate behavior, securities' prices, equity and bond markets, and the overall economy.

In selecting equities for the Strategy, the team uses a combination of investment methods to identify equities that the team believes present attractive return potential. Some of these methods evaluate individual equities or a group of equities based on the ratio of their price relative to historical financial information and forecasted financial information, such as book value, cash flow, and earnings, and a comparison of these ratios to industry or market averages or to their own history. Other methods focus on patterns of information, such as price movement or volatility of a security or group of securities relative to the Strategy's investment universe or corporate behavior of an issuer. The team also may adjust the Strategy's portfolio for factors such as position size, market capitalization, and exposure to groups such as industry, sector, country, and currency.

The resulting portfolio reflects the team's assessment of the best investment opportunities within the Strategy's investment universe and takes into consideration factors such as liquidity, transaction costs, and client mandate requirements.

### **Portfolio Construction**

GMO believes the best form of portfolio management is an understanding and frequent examination of the underlying models and inputs used to generate portfolios.

Security weights are primarily a by-product of our security selection process. Position sizes and group exposures, both absolute and relative to the broad market, are monitored and reviewed by the portfolio management team.

The Strategy typically invests directly and indirectly (e.g., through underlying funds or derivatives) in equities of companies based around the world. Derivatives used may include futures, options, forward currency contracts, and swap contracts.

The Strategy is managed to remain fully invested (typically less than 10% allocations to cash).

*Last Updated: September 30, 2013*

# GMO

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