Shetland
Islands Council

REPORT

To: **Special Shetland Islands Council** **25 May 2010**

From: **Head of Finance**

Pension Fund Management Annual Review 2009/10
Report No: F-025-F

1. Introduction

1.1 The purpose of this report is to inform Members on the position and performance of the Council's Pension Fund external investments with fund managers.

1.2 The Pension Fund has three fund managers with total investments, under management at the end of March 2010, of £222 million.

Funds under Management at 31 March 2010

Manager	Fund	% of Reserves
BlackRock previously Barclays Global Investors (BGI)	Equity and Bond	92
Schroders	Property	7
Record	Currency	1

1.3 BlackRock, Schroders and Record will all give presentations at this Council meeting concerning their investment performance over the year to end March 2010.

1.4 Karen Thrumble will attend the meeting from WM Company, which is part of State Street. WM Company are performance analysts and they independently monitor and report to the Pension Fund on each investment manager's performance. Karen will analyse each fund manager's performance relative to the markets they invest in, before that Fund Manager's presentation to the Council.

1.5 Along with this report are attached the presentational documents from BlackRock, Schroders and Record plus a performance report from the WM Company on the relevant funds.

1.6 In this report I will review each fund manager in turn and compare their performance in 2009/10 against the market performance where they were asked to invest, and also against the additional out performance target we asked them to achieve.

1.7 Due to the nature of the investments these managers are investing into, we take a long-term investment view, generally a five-year period. I will therefore not only look at each manager's performance over 2009/10 but I will also look at their performance over a five-year period, or from the inception of the mandate if that is shorter.

2. Links to Corporate Priorities

2.1 This report links to the Council's corporate priorities, defined in its Corporate Plan, specifically in relation to assisting the Council in ensuring the financial resources are managed so that the Council can sustain and develop the economy.

3. Risk Assessment

3.1 There is no risk associated with this report, as no decisions are required to be made. All investments carry some degree of investment risk but this can be minimised through diversification of fund managers, assets, benchmarks, markets, size of holdings etc.

4. Background

4.1 The Council's Pension Fund is in a growth phase where income from Council and Employee contributions is projected to exceed expenditure for some time to come. Consequently, a long-term investment strategy is appropriate. This allows us to have a higher percentage of equity investments, which in itself produces a greater volatility of returns over the short to medium term, i.e. 1-3 years. Over the long term this investment policy has proved beneficial with the Pension Fund up 49% over the last 5 years and up 116% over the last 10 years.

4.2 At the last actuarial review in 2008 the Pension Fund was 88% funded and was one of the best funded Local Authority Pension Funds in Scotland. This funding position allows the Council to have one of the lowest levels of employer contributions in Scotland (15.5% in 2009/10).

4.3 BGI / BlackRock were used initially for a holding position until a full review of the Pension Fund investment strategy could be conducted. In 2009 it transpired that the Scottish Government had asked the Improvement Service to conduct a review of the Scottish Local Government Pension Scheme, to look at both investment and administrative services. The idea was to see if there were alternative ways to manage these services, i.e. one large centrally controlled Scottish Pension Fund, or perhaps only a few funds, e.g. two or three large Pension Funds. The review in 2009 looked at how the eleven Scottish Pension Funds managed their investments and their administration services. Hymans Robertson collated the initial data from the eleven Local Authority Schemes and analysed it for the Improvement Service. The final report was inconclusive with no guarantee that investment costs could be saved or returns increased with a different Scottish Pension set up. Nevertheless the Scottish Government are progressing in 2010 with phase two, with the sole remit to see if there is an organisation in Scotland which could operate the investment and administration services of one large Scottish Pension Scheme. The results of this are due around the end of 2010. In light of this ongoing Scottish Government project we have effectively put our investment strategy review on hold, at least until the outcome of phase two of the project is known.

4.4 The external investments of the Pension Fund (ie other than those invested in the local economy) are co-ordinated by the Council's Treasury function. The Council and Charitable Trust's reserves, although not covered by this report, are also co-ordinated by the Council's Treasury function. This approach delivers a unified approach; ensures that all the funds benefit from the knowledge and experience of Council Officers; and provides useful comparisons.

4.5 The Funds, their managers, type of mandate and market value are listed below:

		Market Value (£m)	
Manager	Mandate	2010	2009
BlackRock / BGI	Equity and Bonds	204	136
Schroders	Property	16	9
Record	Currency	2	2
		222	147

4.6 During 2009/10 the value of the Pension Fund increased by £75 million.

4.7 In the main, this report concentrates on manager performance relative to the markets but we also need to consider the effect of any cash withdrawals or injections to the funds and the performance of the markets themselves. These influences can easily alter the absolute fund value.

4.8 The following table shows the effect on the fund due to withdrawals/additions and the investment return.

	Pension Fund £ million
As at 31.03.09	147
(Withdrawals)/Additions	8
Investment Return	67
As at 31.3.10	222

The figures show how the investment return of £67 million has benefited the overall investments during the year. This is a remarkable investment return, 46% on the opening investment value. It also shows the volatile nature of investing over the short term, while over the long term the returns are netted off to give a more balanced long-term figure. The Pension Fund has a 75% allocation to equities as the Pension Fund can take a long-term investment outlook. This large allocation to equities was the main contributor to the increase in value of the Pension Fund, which is a direct consequence of the world's major economies coming out of the recent economic recession. The £8 million of additions is due to the difference between the employer and employee contributions versus the pension payments during the year.

4.9 The 2009/10 market performance by asset class is set out below:

		%
Equities:	UK	52.3
	North America	43.2
	Europe	48.8
	Japan	29.6
	Pacific (Ex Japan)	67.2
	Emerging	74.5
Bonds:	UK	0.8
	UK Corporate	31.1
	Index-Linked	10.3
Property		16.3
Cash		0.4

4.10 As can be seen from the asset returns in 2009/10 equities produced some stellar returns with almost all regions returning over 40%, with the UK returning 52.3% and Pacific (Ex Japan) 67.2%. The fund manager has negligible influence over the market's return but they may be required by the mandate agreement to invest into these markets. The main constituent of a fund's performance is the market return, where the fund is invested. A fund manager is only asked to out perform the market return, i.e. a European equity scenario in 2009/10 where a fund manager is asked to out perform the market by 1% would equate to a 49.8% return.

4.11 This report reviews performance in 2009/10; a quick update for the start of this financial year 2010/11 shows a rather more unsettled global economic situation, with concerns over economies such as Greece, Portugal and Spain dominating market sentiment.

5. Fund Manager Review

5.1 The rest of this report takes each mandate in turn and discusses manager performance.

5.2 A Fund Manager's performance is measured against a specific fund benchmark, which is made up of market indices of the countries where they invest.

5.3 A Fund Manager's target is a level of out performance above the benchmark that is seen as achievable with a low level of measured risk on a given mandate. The Manager will actively seek to produce investment returns in order to achieve the stated target. Performance at or above target is desirable but any returns above the benchmark will add value to the fund above the market return.

5.4 <u>BGI / BlackRock - Equity and Bond Fund</u>

5.4.1 During the financial year many of the UK's main banks were selling off any non-core assets to raise cash, rationalise the business etc. Barclays Bank was no exception and sold their fund management business BGI to BlackRock. BlackRock were initially a large US fund management business but over the past few years they have acquired Merrill Lynch and now BGI, to become one of the largest global fund managers.

5.4.2 Any change to a fund manager is monitored closely. The Charitable Trust's investment consultants Hymans Robertson were consulted and they were comfortable with the purchase of BGI by BlackRock. BlackRock are any active investment manager so their purchase of BGI, a passive fund manager, fits well into the overall company with no disruption to BGI's operations. A passive investment process is predominately computer controlled and as expected no issues or problems have occurred. In fact the larger BlackRock business may produce investment opportunities for the Pension Fund.

5.4.3 BGI / BlackRock are the Pension Fund's transition manager and in that role they have the capability to hold funds on a passive basis, i.e. track the market indexes. The Pension Fund is currently making use of this facility, after the decision (min ref 160/08) to terminate Capital International's management of the mandate. This situation will continue until results of the Scottish Government Pension project are known.

5.4.4 Even though BGI / BlackRock is investing the fund passively and it is an interim position this is the Pension Fund's largest mandate

and it is important to meet and question the manager, and to gain an understanding of the company and their investment process.

5.4.5 BGI conducted the transfer of the fund's assets near the end of 2008, with performance monitoring commencing 1st January 2009.

5.4.6 BGI / BlackRock's benchmark for this fund is based on 45% UK Equities, 45% Overseas Equities, 10% bonds. As the fund is invested passively the benchmark and the target are the same, i.e. one aim the index return. For performance comparison purposes the fund return is only compared against the benchmark (index) return. Given the fund is trying to achieve the index return; it is the closeness of the performance to the index which is important. A passive investment is intended to take away the manager risk and just have a market return risk, which over the long term generally provides a positive return.

5.4.7 The following table sets out in summary the performance of BGI / BlackRock versus the benchmark return for 2009/10 and also on a cumulative basis since January 2009.

Fund Performance versus Benchmark

	Fund Return (%)	Performance v Benchmark (%)
2009/2010	43.8	0.3
One and a quarter years to March 2010	23.9	0.4

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

5.4.8 The equity and bond fund with BGI / BlackRock increased by 43.8% in 2009/10, which is only 0.3% above the benchmark return. This shows the fund has mirrored the market return very closely.

5.4.9 On a cumulative basis over the one and a quarter year rolling monitoring period the fund has increased by 23.9%. BGI / BlackRock have only managed this mandate for a very short period of time and they are close to the benchmark return, which is the aim of the fund.

5.5 Schroders - Property Fund

5.5.1 Schroders were awarded this Property Mandate in March 2007 with the first investments commencing in July 2007.

5.5.2 The benchmark for this fund is based on a 100% UK property investment. The fund manager does however have the scope to invest up to a maximum of 30% of the fund in overseas property if attractive investment opportunities exist. Their performance target for this fund is to beat this specific benchmark by 1.0% per annum.

5.5.3 The following table sets out in summary the performance of Schroders versus the benchmark and the performance target in 2009/10, and also on a cumulative basis since inception.

Fund Performance versus Benchmark and Target

	Fund Return (%)	Performance v Benchmark (%)	Performance v Target (%)
2009/10	-2.4	-12.6	-13.6
July 07 to March 10	-10.2	26.2	22.8

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

The performance v target figure gives the percentage that the fund has out or under performed their set target.

5.5.4 The Property Fund with Schroders fell in value by 2.4% and under performed the benchmark by 12.6% in 2009/10, this during a year where the property market was recovering.

5.5.5 On a cumulative basis over the monitoring period since inception Schroders are still well above the benchmark return by 26.2%. This out performance is in a period where markets have gone down and up in value. The fund has decreased in value since inception by 10.2% but due to Schroders management the fund has not fallen as far as the general property market.

5.5.6 This property mandate was initially for £20 million; currently the fund manager has invested about £16.4 million, as they are being cautious given the recent economic turmoil and its effect on the property market. Schroders are only investing into the property market when they find properties at an attractive valuation and are good long-term investments.

5.6 Record - Currency Fund

5.6.1 Record was awarded this Currency Mandate in March 2007 with the first investments commencing in June 2007.

5.6.2 As this fund invests in currencies there is no standard benchmark that can be used to compare performance against. Record

actually uses the monthly Sterling Inter-Bank Offered Rate (LIBOR) minus 0.10% as a performance target. This is the return that I will also review this mandate against, as it is an alternative cash rate to what could have been achieved if the investment was held in a cash product.

5.6.3 The following table sets out in summary the performance of Record versus the benchmark in 2009/10, and also on a cumulative basis since inception.

Currency Fund Performance versus Benchmark

	Fund Return (%)	Performance v Benchmark (%)
2009/10	-8.9	-9.4
June 07 – March 10	-57.3	-61.0

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (Cash).

5.6.4 The Currency fund with Record decreased by 8.9% in 2009/10, which was 9.4% below the benchmark return. This is an extremely disappointing performance from Record.

5.6.5 Cumulatively over the two and three quarter year period of this mandate, the fund has decreased in total value by 57.3%, which is 61.0% below the benchmark return for the same period.

5.6.6 This investment is the Pension Scheme's smallest mandate, initially £5 million, due to the volatile nature of currency. Record use a fixed investment process that has performed well over the long term and this investment was made with that long-term investment view.

5.6.7 Due to the historically uncorrelated returns of currency to equities and bonds this investment class was intended as a diversifier to these other asset classes. Nothing about the company has changed during our investment; the investment process, staff and their long-term belief in the currency markets are still the same.

5.6.8 Over most of the three-year period of our investment the world has seen a major economic crises that no asset class could avoid. During this crisis there was a flight to safety and this was also the case with currencies. In each major sector of the world certain currencies, due to their history are seen as safe havens, such as the dollar with western economies and the Yen with Asian economies. Record's investment process is a fixed computer process based on matching interest rate levels to

certain currencies but due to the flight to safe currencies in recent years, Record's long-term investment process has struggled.

5.6.9 The falls recorded by this fund are not unfamiliar to those we have seen in the equity markets, though equities did bounce back in 2009. Currency investing is more volatile hence the smaller fund and large positive and negative returns were expected over the short term. We have not as yet seen interest rates change; all major economies are keeping interest rates low to help their respective countries.

5.6.10 Record did in 2009 alter their investment management fee structure to put the Pension Scheme on a lower fee scale, along with a performance fee, which only starts when the fund recovers all losses from inception. This effectively cut the management fee by 42% until the fund is back to the initial investment level. Record are also giving the Pension Scheme the choice to opt out of performance fees, if the Pension Scheme wishes, once the fund has recovered all losses from inception.

6. Financial Implications

6.1 Performance by a Fund Manager will have long-term financial consequences for the Pension Fund.

6.2 The performance of the Pension Fund may ultimately affect the contribution rate the Council is required to make. This would be an additional cost / saving to the Council's Revenue accounts.

6.3 There are no decisions from this report, so there are no immediate financial consequences.

7. Policy and Delegated Authority

7.1 Day to day responsibility for Fund Management is delegated to the Head of Finance of Executive Services Department and/or his nominees (SIC 25 July 1996 minute reference 97/96). The Council retains responsibility for appointing Fund Managers and for regularly reviewing and questioning a Fund Managers performance (min ref 97/96). This report provides that opportunity.

8. Conclusions

8.1 The Pension Scheme is taking advantage of BGI's ability, now BlackRock, to hold the equity and bond fund and invest it on an index-tracking basis. This allows the Pension Scheme to stay invested in the market place and achieve market returns until the outcome of the Scottish Government's Pension review is known. BGI / BlackRock have managed the fund for fifteen months and, as

expected, have produced a return over this period that is very close to the markets they are investing in.

8.2 Schroders under performed the benchmark and the target in 2009/10 in a rising market, which is disappointing. Cumulatively though over the two and three quarter year monitoring period, which has seen both falling and rising market situations Schroders are still well above the benchmark and the target return.

8.3 The Currency fund with Record fell by 8.9% in 2009/10, a disappointing performance. Record's investment process was not immune to the effects of the economic crisis and a flight to the safe currencies occurred. Record use a strict investment process, which has proved successful over the long term, though over the past few years this flight to safe currencies along with stifled interest rates, has worked against Record's investment process.

8.4 The Pension Fund during 2009/10 increased in value by £75 million, which equates to a 51% increase in its value. The fund's large equity holding being the driver of this performance. The markets realised in 2009 that the major economies would survive the global economic crisis and this boosted the market place, though many issues and problems still exist.

8.5 The Pension Scheme will await the outcome of the Scottish Government's Pension Scheme review before any decisions are made on an investment review.

9. Recommendations

9.1 I recommend the Council note with satisfaction performance of BGI / BlackRock (equity and bond fund) in 2009/10.

9.2 I recommend the Council note with dissatisfaction the performance of Schroders (property fund) and Record (currency fund) in 2009/10.

Date: 14 May 2010
Ref: CAB/DS Rep No: F-025-F

FOR PROFESSIONAL INVESTORS ONLY

Shetland Islands Council

25 May 2010

Barry Keane

BLACKROCK

Agenda

BlackRock Update

Index Investment Philosophy

Market Outlook

Investment Mandates and Portfolio Performance

Appendix

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Products and Services in Multiple Asset Classes and Styles

£2.23 trillion in world-class products across asset classes that span the full risk spectrum

EQUITY	£1,050 Billion
Fundamental Equity	
Scientific Active Equity	
Index Equity	
iShares	

ALTERNATIVES[1]	£69 Billion
BlackRock Alternative Advisors	
Capital Markets	
Global Market Strategies Group	
Proprietary Alpha Strategies	
Real Estate	
iShares	

FIXED INCOME	£703 Billion
Fundamental Fixed Income	
Model-Based Fixed Income	
Index Fixed Income	
iShares	

MULTI-ASSET	£103 Billion
BlackRock Multi-Asset Client Solutions	
Asset Allocation / Balanced	
iShares	

CASH MANAGEMENT	£203 Billion

FINANCIAL MARKETS ADVISORY	£106 Billion

Transition Management	Securities Lending	BlackRock Solutions

[1] *Includes commodity and currency mandates. AUM in GBP as of 31 March 2010. Source: BlackRock*

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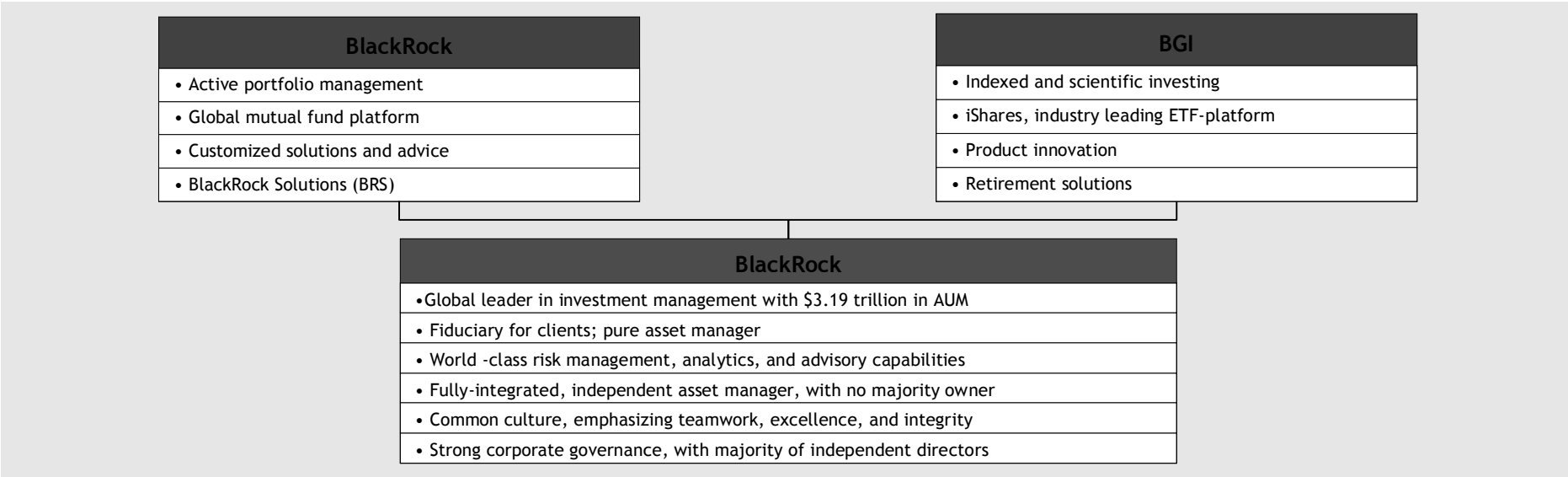
BlackRock/ BGI: Combination of Two Great Firms

On 1 December 2009, BlackRock and Barclays Global Investors (BGI) combined to create a new independent company

- New firm operates under BlackRock

Brings together two market leaders to create extraordinary investment platform

- Unique ability to combine active, enhanced, and index strategies to develop investment solutions for clients
- Market-leading iShares® ETF platform and BlackRock's global mutual funds together create unmatched ability to tailor portfolios for investors
- Market-leading cash management, securities lending, and transition management businesses
- Industry-leading risk management and advisory platform, BlackRock Solutions®, benefits from broader capabilities
- Combined firm is independent and will be fully integrated, with employees, clients and products spanning the globe



Combined AUM in USD as of 30 September 2009

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BlackRock Overview

Independent firm in ownership and governance

- Established in 1988, BlackRock is a public company (NYSE:BLK)
    - No majority owners
    - Majority of Board of Directors is independent
- Laurence Fink, Chairman & CEO since firm's inception

Leader in creating solutions for clients

- Strategies and services differentiated for clients
- Customized solutions to meet risk/return objectives
- Innovative strategies and services within and across asset classes
- Client dialogues have resulted in advisory assignments
- Senior level of commitment to client service
- "One BlackRock" approach results in consistency & quality throughout firm

Pioneer in risk management and technology

- Provides risk management and enterprise investment services for £5.97 trillion in assets
- BlackRock Solutions® offers independent risk management products

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BlackRock Corporate Governance

BlackRock is a publicly-traded company established in 1988

Ownership Structure[1]	34.0% Bank of America 24.3% The PNC Financial Services Group, Inc. 19.7% Barclays PLC 22.0% Institutional investors, employees, and the public
NYSE Listing	BLK (since 1 October 1999)
Board Composition	Majority independent; currently 18 Directors: 2 BlackRock, 2 Bank of America, 2 PNC, 2 Barclays, 10 independents
Board Members	Laurence Fink, Abdlatif Al-Hamad*, Mathis Cabiallavetta*, Dennis Dammerman*, Bill Demchak, Robert Diamond, Kenneth Dunn*, Murry Gerber*, James Grosfeld*, Robert Kapito, David Komansky*, Sallie Krawcheck, Mark Linsz, Sir Deryck Maughan*, Thomas O'Brien*, Linda Gosden Robinson*, James Rohr, John Varley
Chairman & CEO	Laurence Fink
President	Robert Kapito
Office of the Chairman	Laurence Fink (Chairman & CEO), Rob Kapito (President), Rob Fairbairn (Vice Chairman), Blake Grossman (Vice Chairman), Charlie Hallac (Vice Chairman), Richard Kushel (Vice Chairman), Sue Wagner (Vice Chairman), Kendrick Wilson (Vice Chairman)

** independent*

[1] Denotes approximate economic ownership interest as of 28 February 2010. The approximate breakdown for voting common stock is as follows: Bank of America owns 3.7%, PNC owns 35.0%, Barclays owns 4.8%, and institutional investors, employees and the public own 56.5%.

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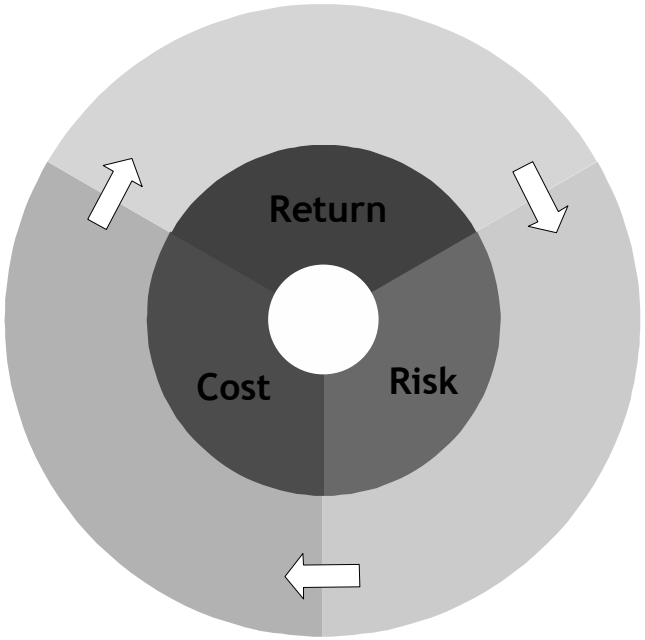
Index Investment Philosophy

Total Performance Management

Core indexing investment philosophy

- Minimising costs is vital
  - Crossing enabled by scale and scope
  - Superior global trading and research
- Controlling investment and operational risks
  - Full replication where practical
  - Robust operational risk controls
- Identifying opportunities to improve returns
  - Value-added portfolio management
  - Flexible strategies and solutions
  - Steady performance with no surprises



Delivering superior risk-adjusted returns

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Minimising Costs

Smart trading saves you a small fortune

- Index funds are always chasing the index
  - Benchmarks assume zero costs
- Maximising crossing limits market trades
  - Size and diversity of global client base
- Careful market trading keeps value in your fund
  - Our global scale keeps costs low
  - Focused trading research ensures quality execution
- Improving portfolio efficiency
  - Use of new tools and instruments

Explicit costs

Implicit costs

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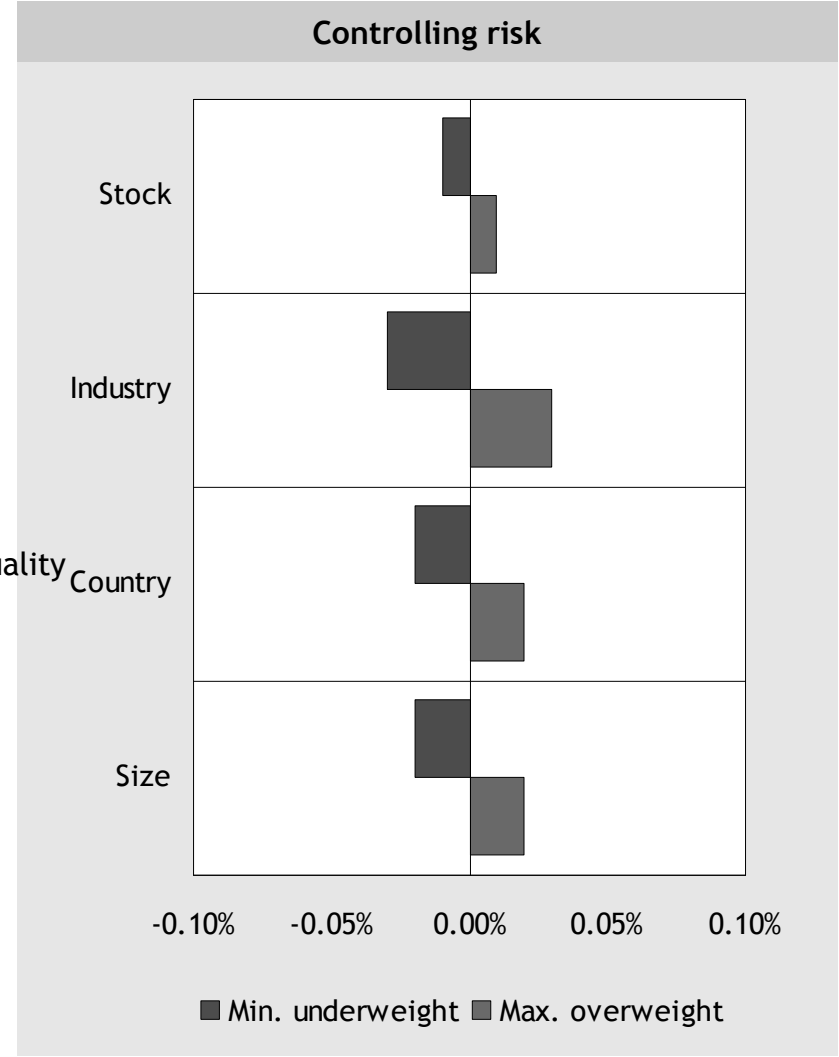
Investment Risk is Tightly Controlled

No surprises

- Two main methods of building index-tracking portfolios
  - Full replication,
    - e.g. developed markets equities, UK bonds
  - Stratified sampling/optimisation,
    - e.g. emerging markets, global bonds
- Minimise risk by closely replicating characteristics of index
  - Security, industry, country and size for equities
  - Currency/country, duration, maturity, industry and credit quality for bonds
- Manage risk/cost trade-off
  - Preserve value in funds



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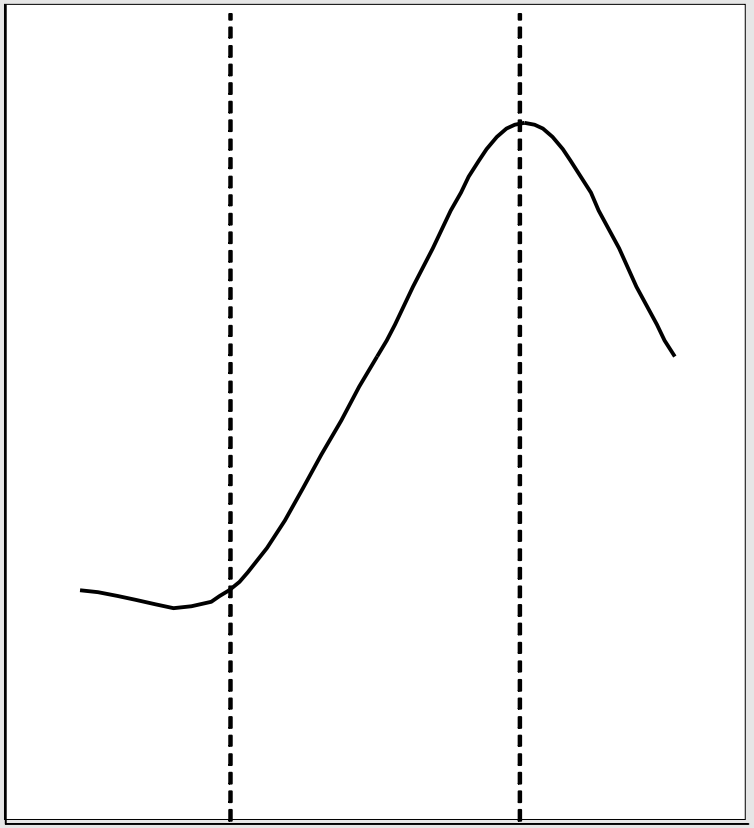
Improving Returns

Helping re-coup costs and maintain economic value

- Pro-active approach to index events
  - Projecting index changes onto portfolios in advance
  - Developing risk controlled strategies
  - Leveraging global trading knowledge
- Understanding the index providers
  - Index construction methodology
  - Providing practitioners' advice on index advisory boards

Index changes – predictable or not?



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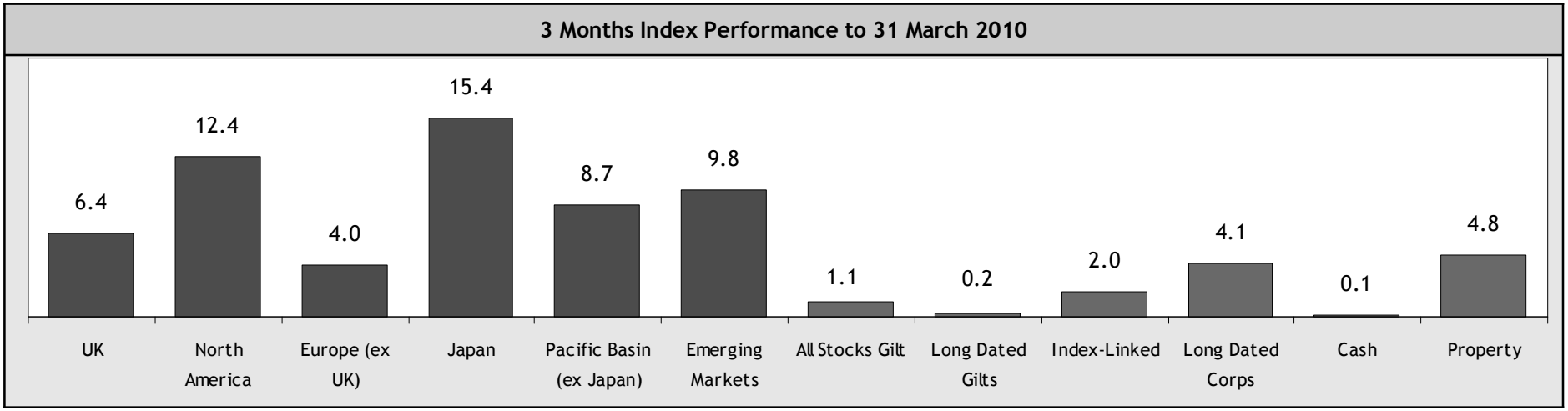
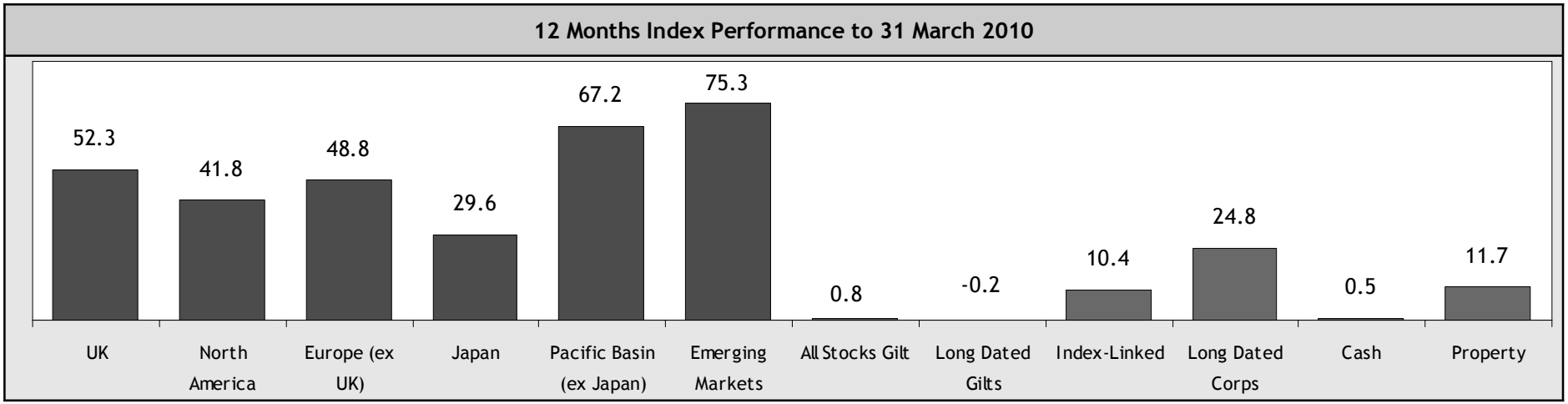
Market Outlook

Market Returns to 31 March 2010





As of 31 March 2010. All returns shown in sterling, total return. UK = FTSE All-Share Index, North America = FTSE World United States Index, Europe (ex UK) = FTSE World Europe (ex UK) Index, Japan = FSTE World Japan Index, Pacific Basin = FTSE World Asia Pacific (ex Japan) Index, Emerging Markets = MSCI EMF (ex Taiwan and Korea) Index, All Stocks Gilts = FTSE A UK Gilts All Stocks Index, Long Dated Gilts = FTSE Over 15 Year Gilt Index, Index-Linked = FTSE Over 5 Years Index-Linked Gilt Index, Long Dated Corps = Bank of America (BofA) ML Eurosterling Over 10 Year Index, Cash = 7 Days London Interbank Bid Rate (LIBID), Property = Investment Property Databank (IPD) All Balanced Property Funds Weighted Average. Source: BlackRock

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First Quarter Market Background

Equity market rally continues

- Developed equities slightly outperform emerging markets

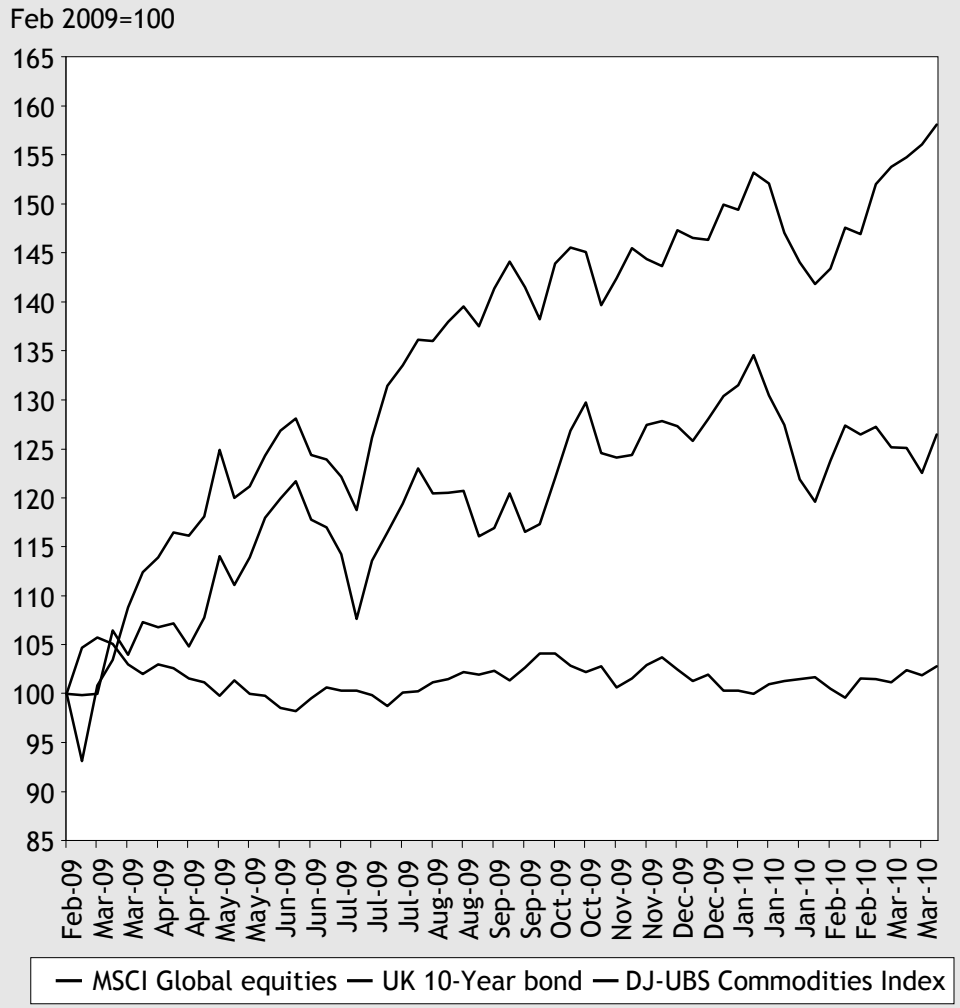
Government bond yields range-bound

- Material stresses in Southern Europe

Dollar strength against European currencies

Moderate gains in commodity prices

Asset class returns since Feb 2009



Source: BlackRock/Datastream

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Economic Environment Update

Underlying fundamentals continue to improve, but concerns over fiscal deficits

US

- Manufacturing survey continues to improve led by new orders & export growth
- US unemployment starting to stabilise, core inflation declining; Fed remains on hold for now.

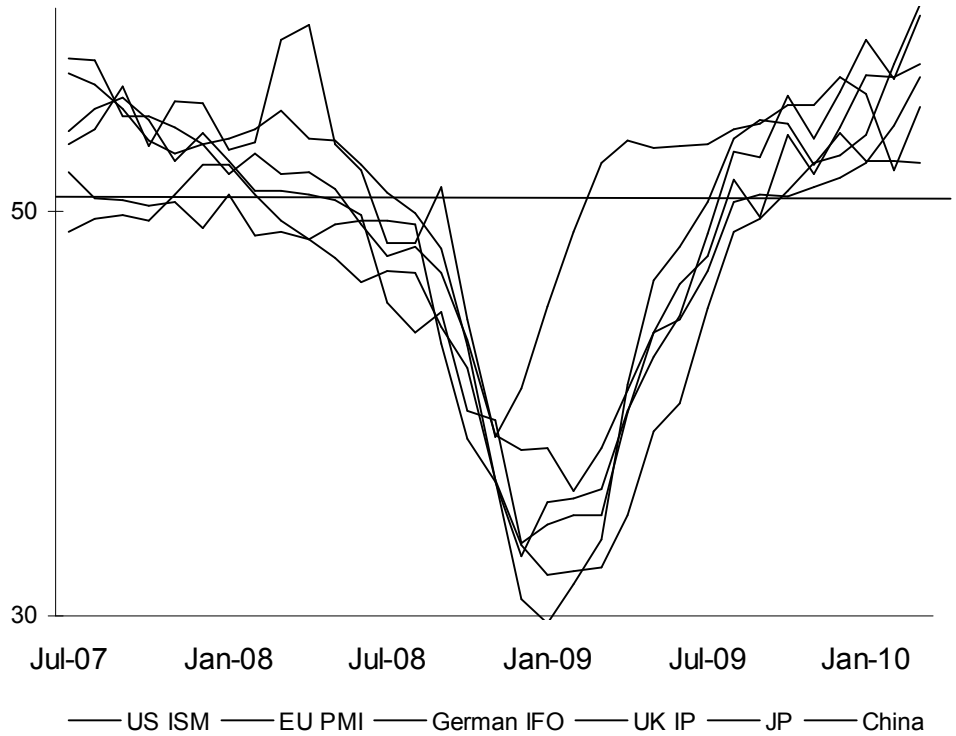
Europe/UK

- Positive growth in Germany, France & Italy but peripheral Europe still sluggish
- Fiscal problems escalate in Greece, pending EU & IMF bailout
- Concerns over UK fiscal deficits & election outcome

Australia/Asia

- China continues to growth strongly forcing PBOC to raise reserve ratio's in Jan & Feb.
- Australian; RBA continues to raise rates 0.50bp in 2010
- Japan's PMI's improving but deflation still the major concern

Manufacturing surveys continue to improve



Source: DataStream and BGI research

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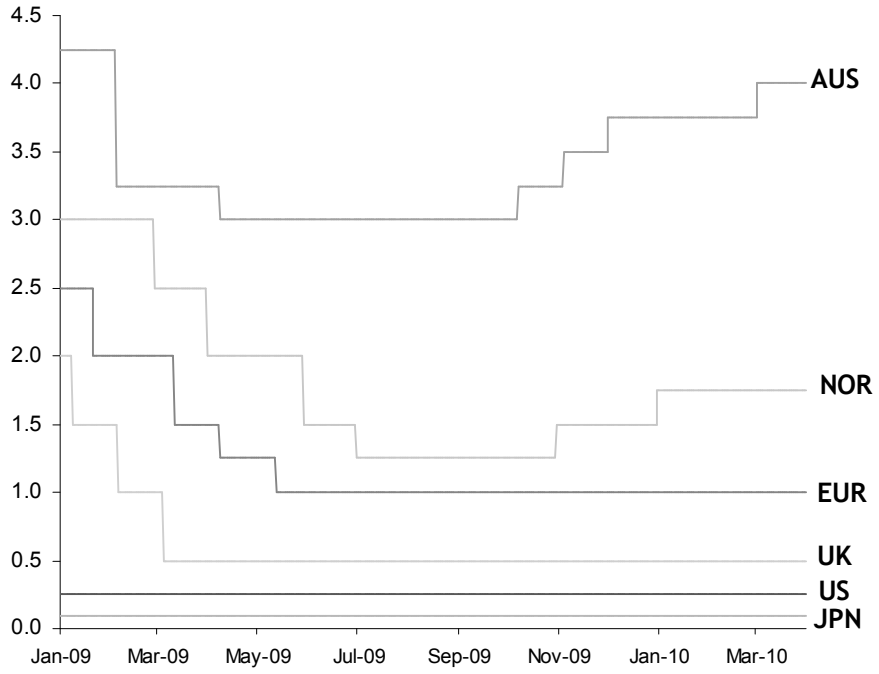
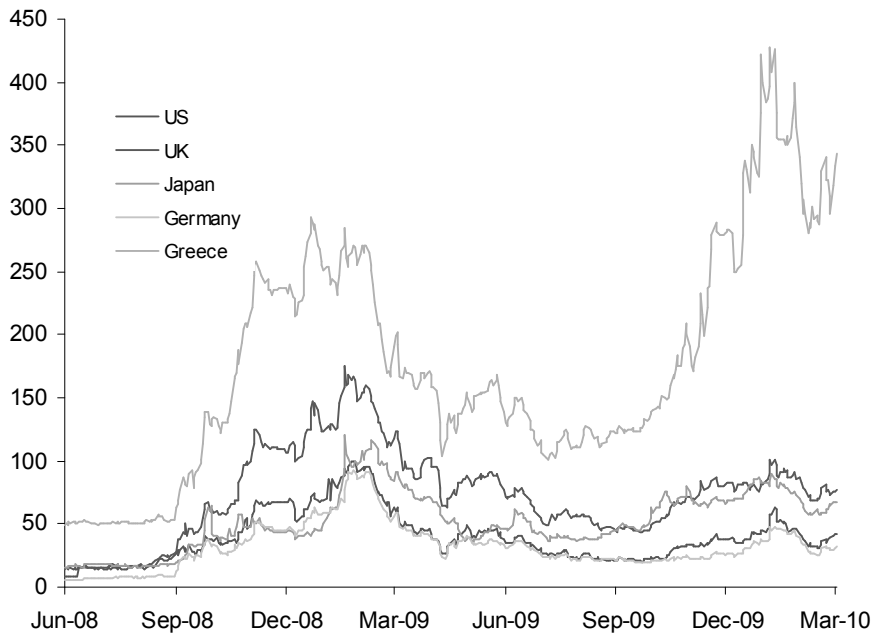
Monetary and Fiscal Policy Both in Focus

Central Bank Policy Rates



CDS Spreads on Sovereigns



- G3 CB rates still at historically low levels, expect some unwind later this year
- RBA continues to raise rates, others may follow

- Increased risk of sovereign debt default pushes up cost of CDS
- Greece fiscal concerns escalate in Q1 with pending EU & IMF bailout

813369

Source: Datastream, IMF

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Investment Mandates and Portfolio Performance

Shetland Islands Council Pension Fund

BlackRock's investment mandate and position at 31 March 2010

Fund Name/ Asset Class (%)	Benchmark Allocation	Tolerance	Actual Allocation
Aquila Life UK Equities	42.9	+/-1.5	41.9
ISF Europe ex-UK Equities	14.0	+/-1.5	14.1
ISF North American Equities	9.9	+/-1.5	10.0
ISF Japanese Equities	9.5	+/-1.5	10.2
ISF Pac Basin ex Japan Equities	9.5	+/-1.5	10.1
Gilts (Gilttrak)	5.0	+/-1.5	4.3
BlackRock UK Corporate Bond Index Fund	5.0	+/-1.5	4.3
BlackRock Sterling liquidity First Fund	4.2	+/-1.5	3.6
Cash	0.0		1.5
Total	**100.0**		**100.0**

Portfolio value as at 31 March 2010: £202.3m

Source: BlackRock

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BLACKROCK

Shetland Islands Council Pension Fund

Portfolio Performance to 31 March 2010

Pension Fund portfolio has a 15 month history — inception date 31 December 2008

15 month account return of 23.9% in line with benchmark return of 23.5%

Returns (%)	Account	Fund	Index
Aquila Life UK Equities	29.89	29.96	29.74
ISF Europe ex-UK Equities	18.32	18.32	17.76
ISF North American Equities	22.09	22.13	22.02
ISF Japanese Equities	7.05	7.15	7.10
ISF Pac Basin ex Japan Equities	51.87	52.11	52.07
Gilts (Gilttrak)	-0.30	-0.29	-0.03
BlackRock UK Corporate Bond Index Fund	12.03	12.09	11.95
BlackRock Sterling Liquidity First Fund	0.67	0.68	0.54
Total Fund	**23.89**		**23.48**

Source: BlackRock

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Shetland Charitable Trust

BlackRock's investment mandate and position at 31 March 2010

Fund Name/ Asset Class (%)	Benchmark Allocation	Tolerance	Actual Allocation
UK Equities (Charitrak)	50.00	+/-1.5	50.04
ISF Europe ex-UK Equities	16.67	+/-1.5	16.51
ISF North American Equities	16.67	+/-1.5	16.79
ISF Japanese Equities	8.33	+/-1.5	8.27
ISF Pac Basin ex Japan Equities	8.33	+/-1.5	8.39
Cash	0.00	+/-1.5	0.00
Total	**100.0**		**100.0**

Similar funds as used by the Pension Fund

- No bond funds
- Different charity-specific UK equity fund
- Same overseas equity funds

Portfolio value as at 31 March 2010: £118.5m

Source: BlackRock

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Shetland Charitable Trust

Portfolio Performance to 31 March 2010

Charitable Trust portfolio has a 18 month history — inception date 30 September 2008

18 month account return of 26.2% in line with benchmark return of 26.3%

Returns (%)	Account	Fund	Index
Charitrak (UK equities)	29.30	29.34	29.74
ISF Europe ex-UK Equities	18.33	18.32	17.76
ISF North American Equities	21.98	22.13	22.02
ISF Japanese Equities	7.12	7.15	7.10
ISF Pac Basin ex Japan Equities	52.05	52.11	52.07
Total Fund	**26.17**		**26.32**

Source: BlackRock

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Aquila Life Q1 2010 Fund Performance and Attribution

Funds	Fund performance (%)	Index performance (%)	Difference (%)	Comments
UK	+6.43	+6.42	+0.01	+0.5 bp lending, +0.5 bp trading and index changes
Europe x UK	+3.87	+3.83	+0.04	+1.6 bps efficient trading, +1.4 bps lending and TRS, +0.5 bp compounding
US	+12.40	+12.39	+0.01	+0.03 bp lending, +0.03 bp trading and index changes, +0.03 bp futures mistracking
Japan	+15.44	+15.35	+0.09	+0.4 bp lending, +9.6 bps early div. accrual, -1 bp reversion from 2009
Pacific Rim x Japan	+9.61	+9.69	-0.08	+2 bps lending, -10 bps div. accrual reversal

Source: BlackRock and FTSE as at March 2010. Aquila Life funds are benchmarked to the FTSE Net Indices.
Past performance is not a reliable indicator of future results.

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Index Selection Q1 2010 Fund Performance and Attribution

Funds	Fund performance (%)	Index performance (%)	Difference (%)	Comments
UK	+5.83	+5.82	+0.01	+2bps Royal Dutch Shell non UK holding, -1bp administrator fees & other costs.
Europe x UK	+3.62	+3.51	+0.11	+9bps sec lending, +2bps trading & index changes, +1bp tax advantage, -1bp administrator fees & other costs.
North America	+5.34	+5.34	+0.00	+1bp trading & index changes, -1bp administrator fees & other costs.
Japan	+8.20	+8.18	+0.02	+3bps trading and index changes, -1bp administrator fees & other costs.
Pacific Rim x Japan	+3.08	+3.10	-0.02	-1bp trading and index changes, -1bp administrator fees & other costs.
EMU	+1.02	+0.92	+0.10	+9bps sec lending, +1bp trading & index changes, +1bp tax advantage, -1bp administrator fees & other costs.

Source: BlackRock and MSCI as at 31 March 2010. Index Selection Funds are benchmarked to the MSCI Net Indices.
Past performance is not a reliable indicator of future results.

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Economic & Market Outlook

Global recovery theme now more firmly established

- Growth to continue into second half of year, though boom unlikely

Policy stimulus still largely in place

- Central bank asset purchases coming to an end, but sales will be spread over long period
- Interest rates to remain on hold at very low levels

Inflation rises primarily commodity-price driven

- Muted growth prospects and substantial excess capacity likely to see levels decline

UK general election 6 May 2010

- Given range of potential outcomes, gilt yield volatility likely to increase as the election draws nearer
- Political uncertainty could see volatility in UK equities, though market's exposure to overseas earnings is helpful

Risk assets attractively valued versus defensive assets

- We continue to favour equities, credit and commodities over government bonds and cash

Source: BlackRock

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Appendix

Current Client Trends

- **Review of Risk Budget & De-risking**
  - LDI
  - Journey Management
- **Specialist concentrated equity strategies**
- **New or additional allocations to property**
- **Increasing appetite for alternatives generally**
- **Diversified growth strategies**
- **Fiduciary management**

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BLACKROCK

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Shetland Islands Council Pension Scheme

Q1 2010 Property Mandate Investment Review Meeting

Geoff Day – Client Director
Jenny Buck – Head of Property Multi-manager

25 May 2010

Additional information: For Professional Investors only. Not Suitable for Retail Clients

Schroders

Agenda

Property market update

Portfolio review

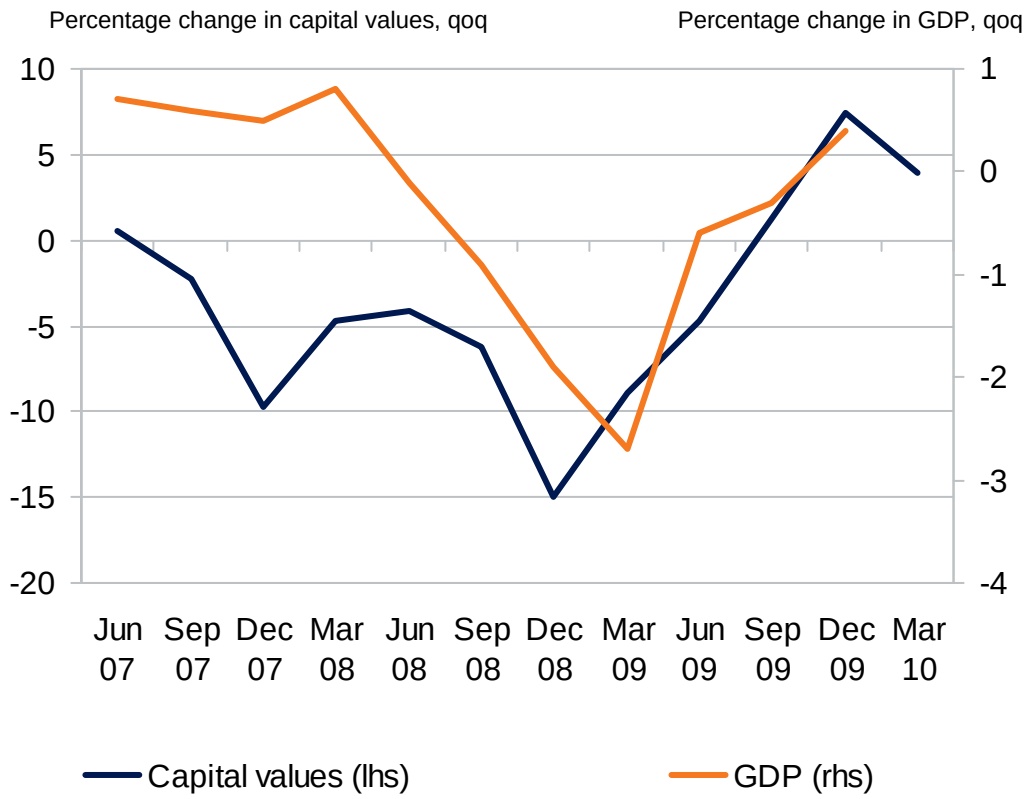
Summary

Schroders

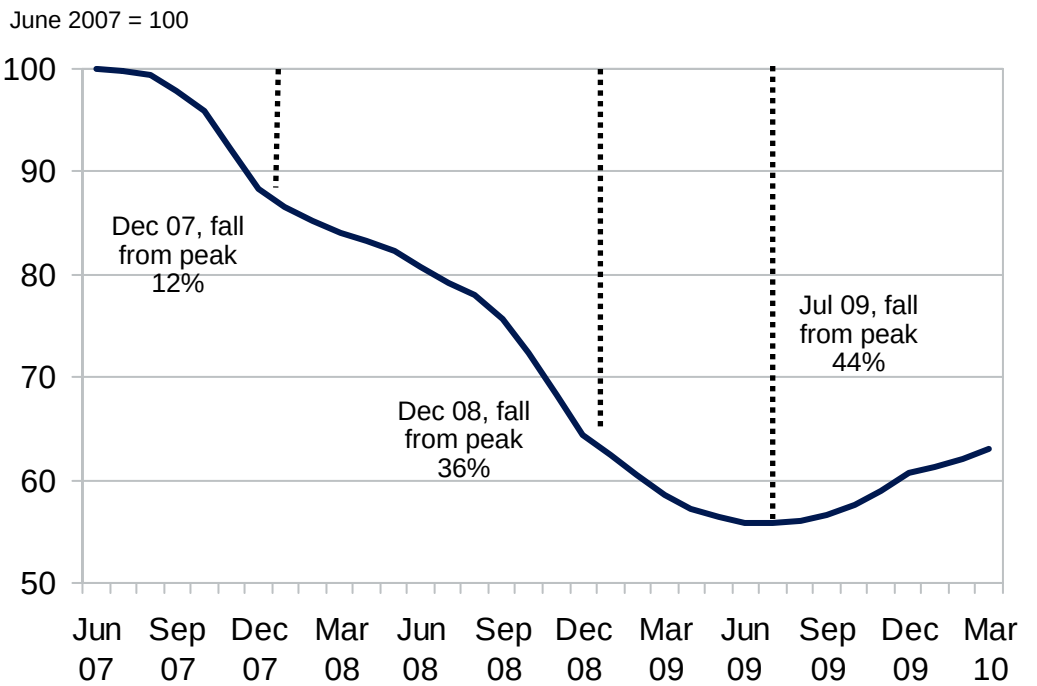
UK commercial property capital values turn the corner

Capital values have risen 13% from the trough

Capital values and economic growth



Capital values

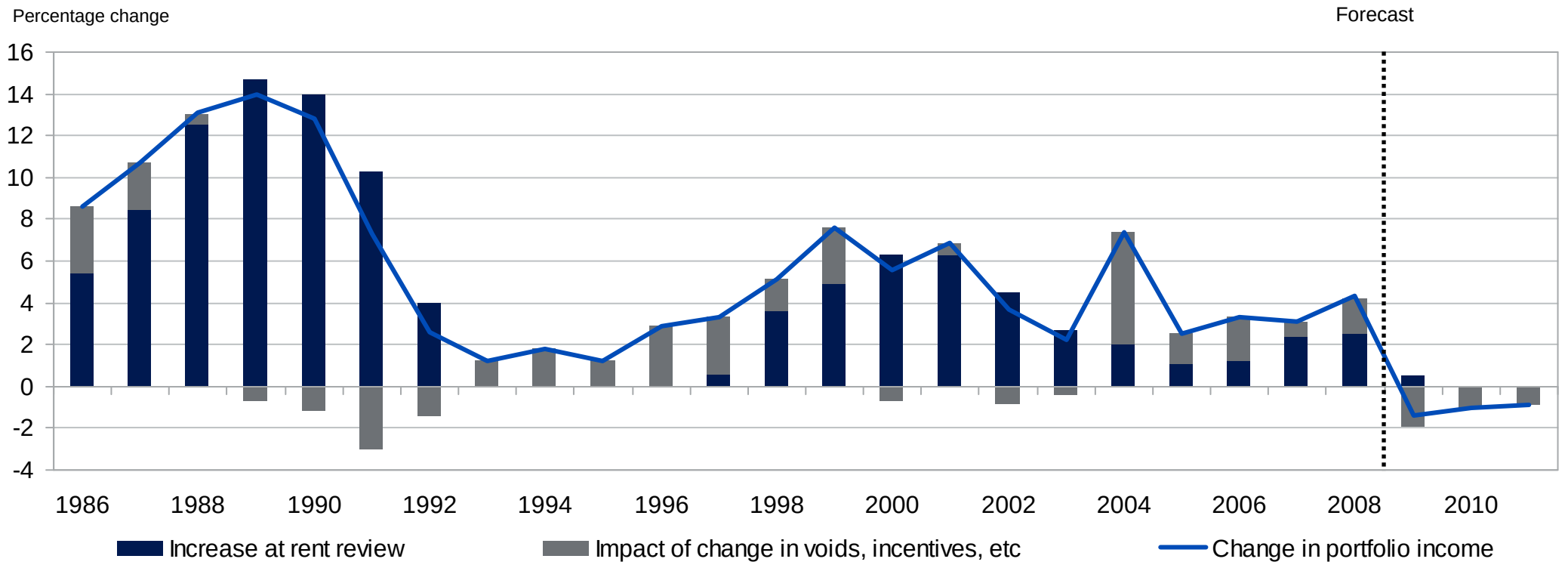


Source: IPD Monthly Index, ONS, Schroders, March 2010

Schroders

Portfolio income has been less secure than in early 1990s

Fall in income reflects fewer reversions and shorter leases



	2008	2009	2010 (forecast)
IPD void rate (%)	8	10	10

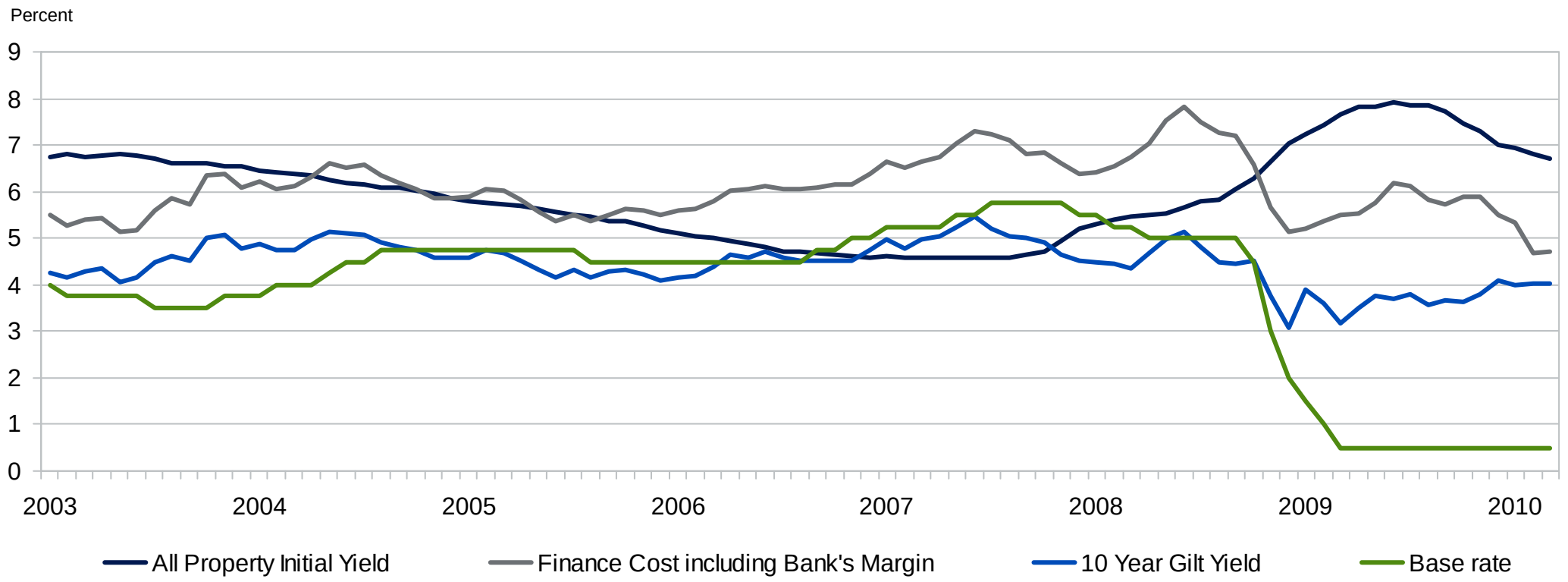
The forecast should be regarded as illustrative of trends. Actual figures will differ from forecasts
Please refer to the Important Information regarding forecasts

Source: IPD, PMA, Schroders, March 2010

Schroders

The UK investor's perspective

Property looks attractively priced relative to bonds and cash

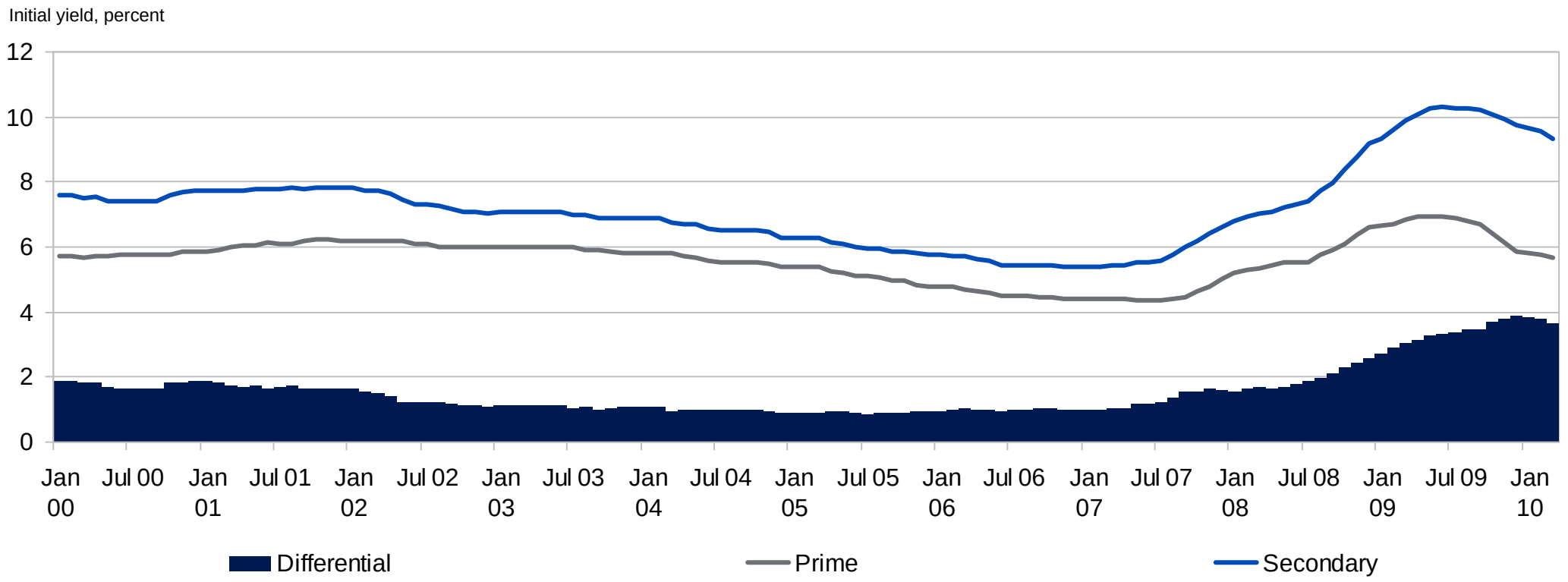


Source: FT, IPD, Schroders, March 2010

Schroders

Prime vs. secondary property yields

Prime properties see the largest fall in yields / rise in capital values



Source: CBRE, March 2010

Schroders

UK property market update

Schroders house view Q1 2010: 3 year view

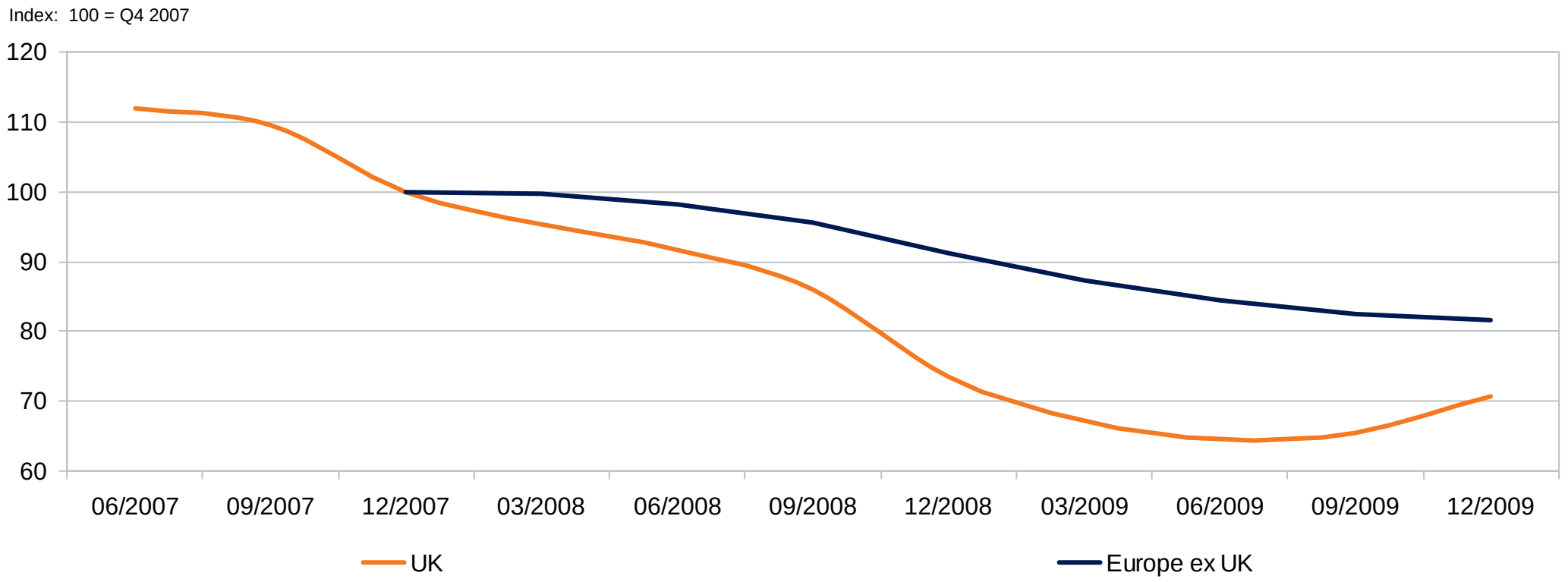
Target	Sector	Expected direction
Very overweight	None	
Overweight	Standard Industrial London & South East	↓
	Offices – Rest of South East	↑
	Standard Industrial Rest of UK	↔
	Offices – City	↑
	Offices West End and Mid Town	↔
Neutral	Cash & Listed	↔
	Alternatives	↔
	Fashion Parks	↔
	Retail Warehouses ex Fashion Parks	↔
Underweight	Shopping Centres	↑
	Distribution Warehouses	↔
Very underweight	Standard Retail	↓
	Offices Rest of UK	↔

Source: Schroders, March 2010

Schroders

Continental European property market

All property capital values



Source: CBRE European Valuation Monitor, March 2010

Schroders

Continental European property market forecast

March 2010

- The Nordic markets, and Eastern Europe, are expected to see relatively strong economic growth
- Retail rents are expected to stabilise in 2010; office rents may decline further
- Prime office yields appear to have peaked in mid 2009 given the revival in investor demand
- Property lending will continue to be tight for the foreseeable future
- On average retail is expected to outperform offices
- Total returns should turn positive in 2010, but are likely to lag the UK

Please refer to the Important Information at the back of this presentation regarding forecasts

Source: Schroders, March 2010

Schroders

Shetland Islands Council

Q1 2010 Property Mandate Investment Review Meeting

Schroders

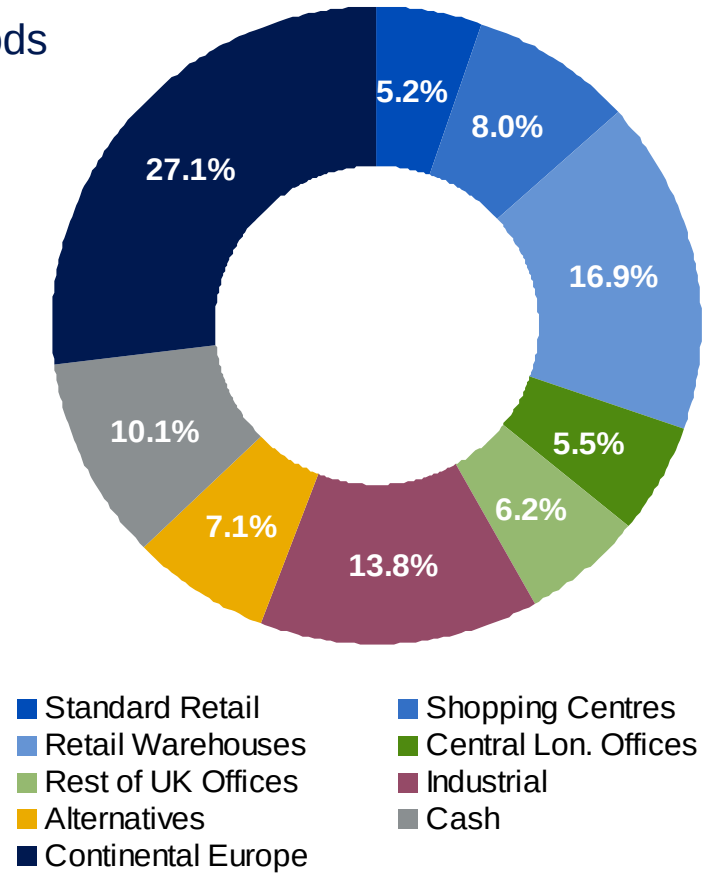
Portfolio review: Shetland Islands Council Pension Scheme

Property portfolio, 31 March 2010

- Benchmark: UK Pooled Property Fund Indices
- Objective: outperform* by 1.0% pa over rolling 3 year periods
- Valuation: £15,621,297, £3.6 million to invest
- Underlying exposure to over £8.6 billion of UK property
- Weighted average yield is 3.3%
- Weighted average debt in funds is 35.4% of NAV
- Portfolio of 9 unlisted property funds and cash, of which:
  - 42.0% core funds
  - 27.2% UK value added funds
  - 27.1% continental Europe value added funds
  - 3.7% cash

* Net of fees

Portfolio sector exposure



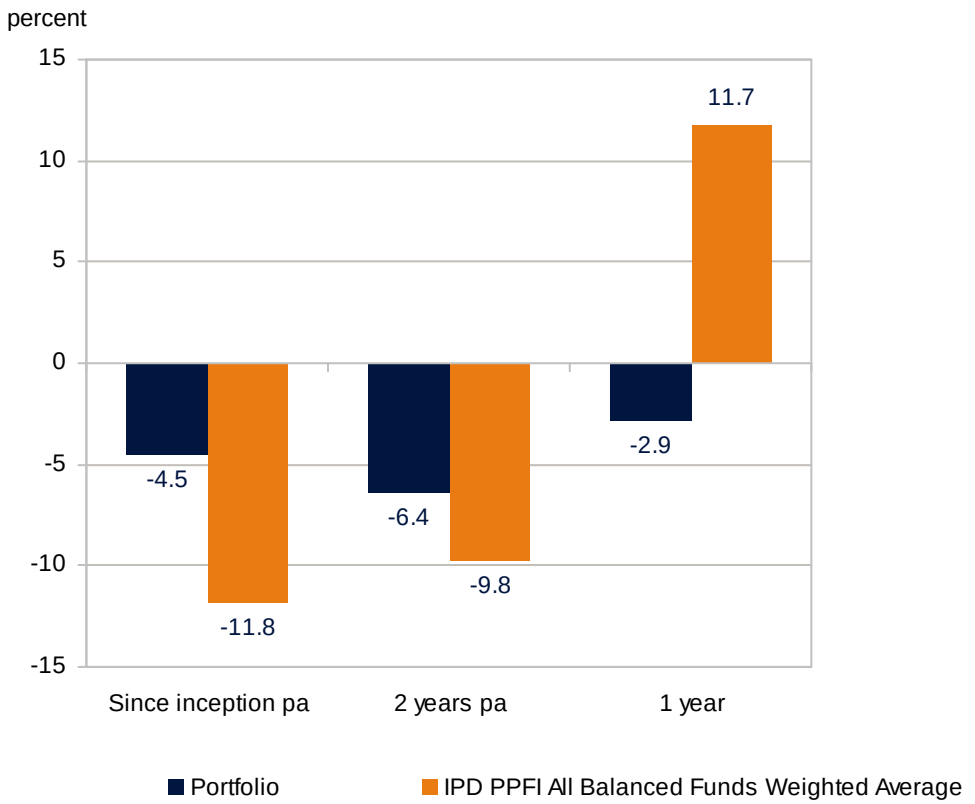
Source: Schroders, March 2010. Data subject to rounding.

Schroders

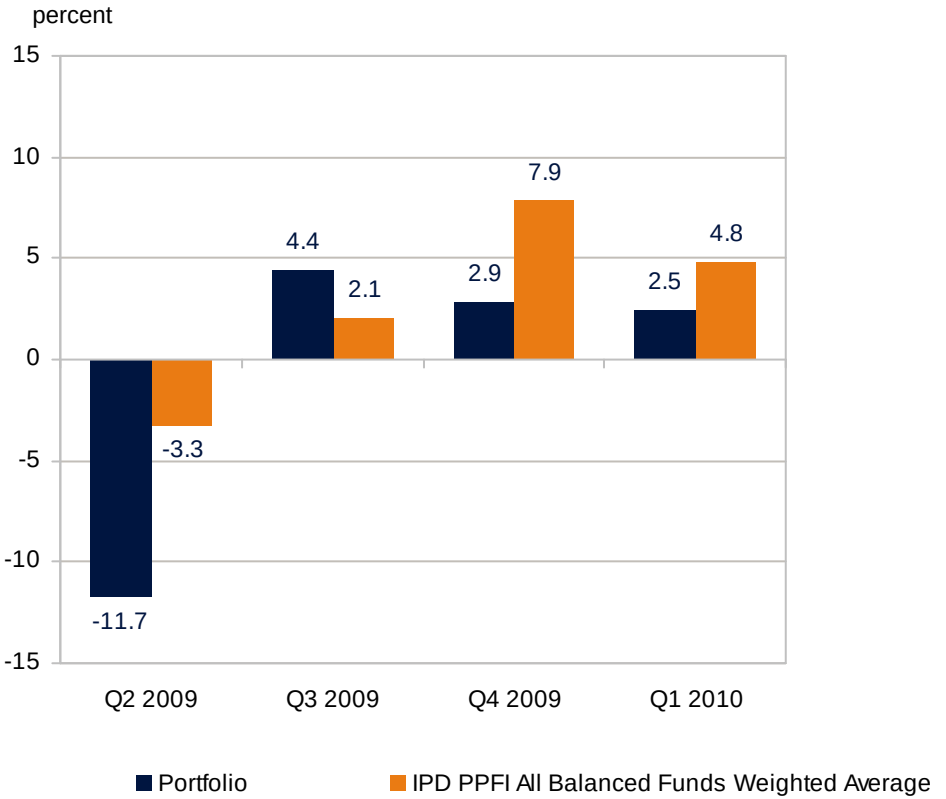
Portfolio review: Shetland Islands Council Pension Scheme

Property portfolio performance – total returns versus benchmark, March 2010

Rolling periods



Past four quarters



The portfolio's returns are calculated on the basis that units in open-ended funds are valued at their mid price and closed-ended funds at their NAV price. Returns are net of multi-manager fees. Benchmark returns for 2 years and since inception are estimated.

Source: Schroders, IPD UK Pooled Property Funds Indices.

Schroders

Portfolio review: Shetland Islands Council Pension Scheme

Performance attribution relative to benchmark

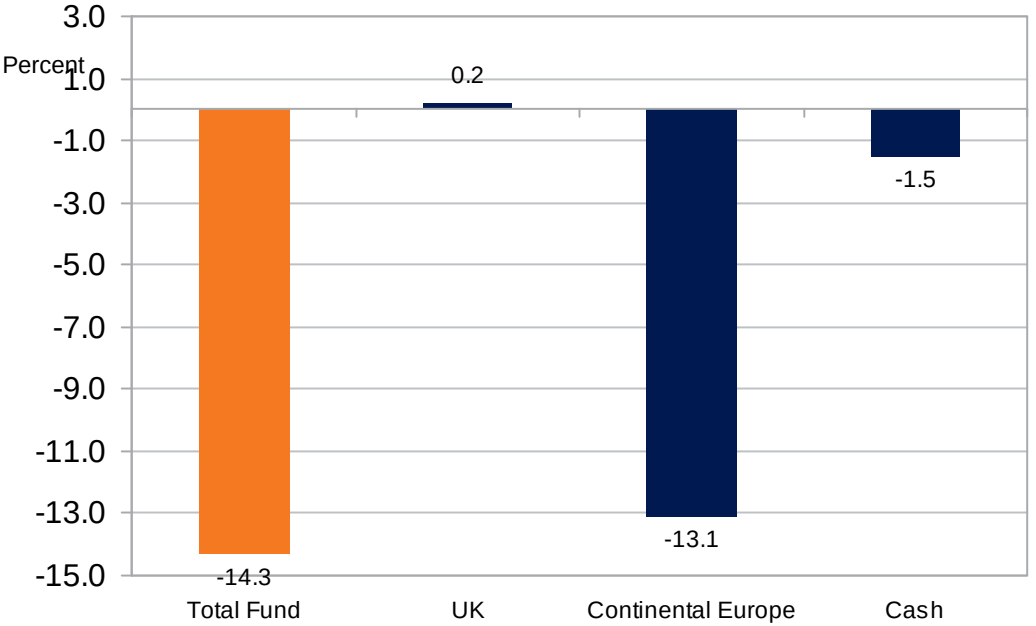
Positive

- Core UK funds were accretive to performance
- Purchases on the secondary market

Negative

- Continental Europe
- Transactions costs on new investments (-0.7%)
- Fund valuation lag (-0.5%)

12 months to 31 March 2010



*Benchmark is UK Pooled Property Fund Indices – All Balanced Funds Weighted Average
Returns are gross of multi-manager fees

Source: Schroders and IPD UK Pooled Property Fund Indices

Schroders

Portfolio review: Shetland Islands Council Pension Scheme

Schroder Real Estate Fund of Funds – Continental European Fund (CEF I)

Actively managed, diversified continental European property fund

- Closed ended fund valued at €198 million
- Substantial cash balance available to exploit opportunities
- Very experienced fund management team
- Valuations are beginning to stabilise

1: CPH Business Park, Copenhagen owned by Valad Nordic Aktiv Property Fund I, 2: 8a Avenida, Portugal, owned by Sierra Portugal Fund, 3: Bergvik Kopcenter, Sweden, owned by Eurocommercial Properties N.V, 4: Baden-Baden, Germany, owned by Henderson HERALD

Source: Schroders, March 2010

Schroders

Portfolio review: Shetland Islands Council Pension Scheme

CEF I performance record to 31 December 2010

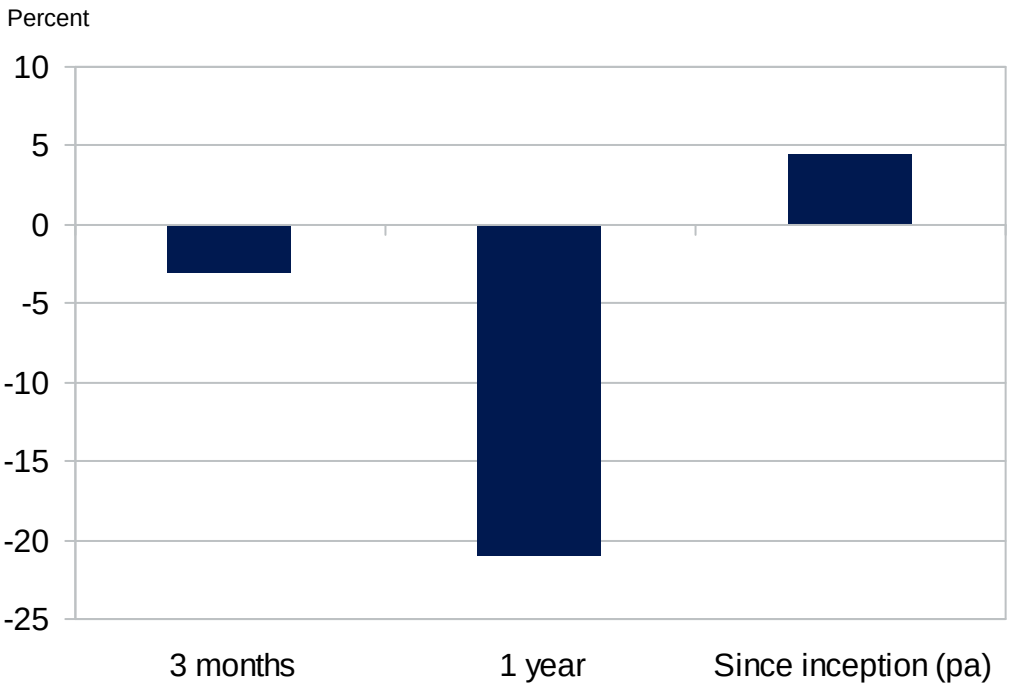
Positive drivers (12m)

- Listed securities and secondary market trades
- Large cash balance

Negative drivers (12m)

- Falling property valuations
- Gearing within funds

Reported sterling returns % to 31 December 2009



Please refer to the Important Information at the back of this document regarding past performance.

Source: Schroders, 31 December 2010. Note: I units, Inception date 18 December 2006. Performance calculated net of fees on a NAV to NAV basis plus income

Schroders

Portfolio review: Shetland Islands Council Pension Scheme

CEF I portfolio holdings: Eurocommercial Properties N.V.

Investment description and rationale

– Prime portfolio of retail mainly Italy, France and Sweden

– Impossible to replicate portfolio in private funds

– Solid track record of management team

– Purchased shares at an average price of €20.24

Recent events and outlook:

– After share price rises, forecast IRR now reduced to < 6% p.a. for 5 years

– Sold ± 80% of holding, reinvestment opportunities identified

– Generated €4.9m of profits that was distributed in past six months

Carosello Saturn, Italy

Please refer to the Important Information at the back of this presentation regarding forecasts

Source: Eurocommercial Properties N.V, Schroders, March 2010

Schroders

Portfolio review: Shetland Islands Council Pension Scheme

CEF I portfolio holdings: NREP Logistics AB

Investment description and rationale

- Nordic logistics fund with a seed portfolio of 8 assets
- Logistics market in the region benefits from long lease structures, high current income, limited speculative supply and low vacancies
- Experienced team with good track record
- Projected IRR of 14-16% and high annual distributions

Ahtonkaari 5, Lieto (Turku), Finland

Recent events and outlook:

- We believe Stockholm, Helsinki and Oslo will be among the top 10 fastest growing regions in Europe

Please refer to Important Information regarding forecasts

Source: Schroders, March 2010

Portfolio review: Shetland Islands Council Pension Scheme

UK activity over last 9 months: £6.2 million invested in 6 funds

Legal and General Managed Property Fund

- A mid-sized UK balanced managed property fund
- Nearly a third of the fund in cash on purchase - reflected in the offer price
- No direct gearing or development risk

Blackpole Retail Park, Worcester

Standard Life Pooled Pensions Property Fund

- Highly diversified £1.7 billion UK core property fund
- Units transferred in from Shetland Towage Scheme, and further units bought at mid price in August

Solihull Retail Park

The examples shown above are for illustrative purposes only and are not to be considered a recommendation to buy/sell.

Source: Schroders and IPD UK Pooled Fund Indices, March 2010

Portfolio review: Shetland Islands Council Pension Scheme

UK activity over last 9 months

Henderson UK Retail Warehouse Fund

- £994 million portfolio, predominantly invested in fashion parks which have strong appeal to tenants and shoppers
- We bought units at a 5% premium to the January 2010 net asset value.

The Quarry, Craigleith, Edinburgh

Standard Life UK Shopping Centre Trust

- £1.1 billion portfolio of prime UK shopping centres
- Bought in Q3 2009 at a 9% discount to the end August 2009 valuation

Churchill Square, Brighton

Industrial Property Investment Fund

- A sector specialist industrial fund with a south east bias
- We bought units at a 6.5% premium to the January 2010 net asset value.

West Wiltshire Trading Estate

Threadneedle Strategic IV

- Experienced managers launched new fund in July 2009
- Delayed investment until second closing and achieved the same terms as cornerstone investor. No revaluation of assets. 65% drawn in 3 months

Ryndon Lane Retail Park, Exeter

The examples shown above are for illustrative purposes only and are not to be considered a recommendation to buy/sell.

Source: Schroders and IPD UK Pooled Fund Indices, March 2010

Schroders

Portfolio strategy
May 2010

- To invest the remaining £3.6 million allocated to property in the most cost effective way over the next few months.
- Retain sufficient cash to meet future calls from the Threadneedle Strategic Fund IV.
- Aim to bring the proportion of the portfolio invested in core funds up to over 50%.
- Many open ended, core funds are restricting access. We have secured places on some fund waiting lists, but we are also in due diligence on an additional fund to add to our platform and are working with a manager to create a new core fund specifically for our clients.

Source: Schroders, March 2010.

Schroders

Summary

Property Market

- UK commercial property returns remained strongly positive in the first quarter 2010, after the rebound in the second half of 2009.
- Capital values rose by 13% from June 2009 to March 2010 over the same period; but remain 37% below their peak in June 2007.

Shetland Islands Council Pension Scheme Portfolio

- We have invested £6.2 million into UK property over the last 9 months
- Short term performance has been impacted by continental Europe, which is over 27% of the portfolio
- We aim to build a diversified portfolio, focussing on investing the remaining allocation to property in core, balanced funds

Schroders

Appendices

Your Team at Schroders

Curriculum vitae

Geoff Day – Client Director

Client Director in our dedicated Client Servicing team, based in London
Joined Schroders in 1996
Joined Flemings as a fund manager for pension funds and charity clients in 1987. Investment career commenced in 1980
Degree in Business Studies, University of Plymouth

Tel: 020 7658 3399 **Email:** geoffrey.day@schroders.com

Jenny Buck – Head of Property Multi-Manager

Responsible for Schroders' global property multi-manager business. Joined Schroders in 2001
In 1999 joined Erste Bank as a property banker, responsible for pricing, booking and managing loans as well as buying commercial mortgage backed property bonds.
In 1992 started investment career at Grosvenor Estate where she spent seven years in property asset management and investment covering all the commercial sectors of the UK market as well as the residential sector.
Member of the Investment Property Forum, Senior Vice President of the Cambridge Land Economy Society, member of the Department of Land Economy Real Estate Advisory Board, member of NAPF's Property Committee, and ranked in the Top 100 Women in Finance by the Financial Times in 2008. She is also a Chartered Surveyor.
MA (Hons) in Land Economy, Cambridge University

Tel: 020 7658 3109 **Email:** jenny.buck@schroders.com

Schroders

Curriculum vitae

Jennifer Murray - Property Fund Manager, Multi-Manager

Fund manager for 10 segregated property multi-manager portfolios and fund advisor to The Schroder Indirect Real Estate Fund. Based in London
In 2005 joined Schroders' property multi-manager team. In 2003 became the fund manager of Schroder Emerging Retail Property Unit Trust (SERPUT), an award winning fund. Joined Schroders in 1999, as a retail asset manager for Schroder Exempt Property Unit Trust (SEPUT)
Investment career began in 1994 at Weatherall Green & Smith where she qualified as a chartered surveyor, working in investment valuation, management and agency
Member of the Royal Institution of Chartered Surveyors
MA (Hons) in Geography, University of St Andrews. MSc in Land Management and Development, University of Reading

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Schroders

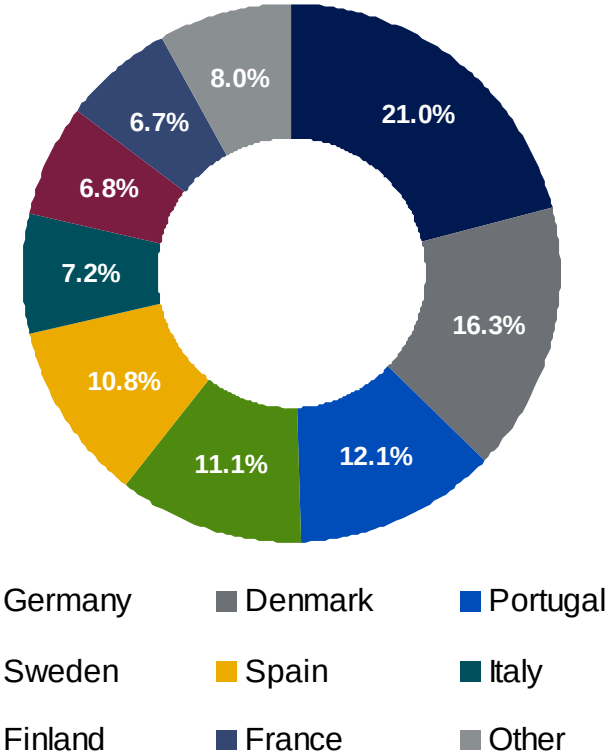
Schroders Real Estate Fund of Funds
Continental European Fund I (CEF I)

Schroders

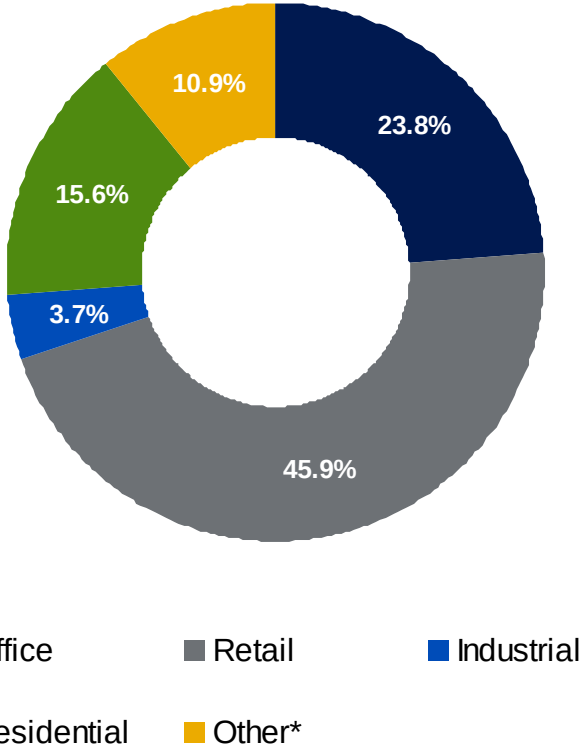
CEF I: portfolio structure

31 March 2010

Country weightings, % NAV



Sector weightings, % NAV



*Includes mainly mixed use assets

Source: Schroders, March 2010

Schroders

CEF I: portfolio holdings

Henderson HERALD

Investment description and rationale

- Pan-European retail fund investing in 22 properties across 9 countries
- Overall fund leverage 49.6%, with substantial cash on balance sheet
- Off market opportunity from a “distressed” seller
- Acquired €3 million of existing units at 42% discount to September 2009 externally valued NAV
- Projected IRR of 18% using conservative assumptions

Baden-Baden, Germany

Recent events and outlook:

- Q4 2009 valuation beginning to stabilise
- Unlikely this deal could be replicated in current market

Please refer to Important Information regarding forecasts

Source: Schroders, December 2009

Schroders

CEF I: portfolio holdings

AXA European Real Estate Opportunity Fund II

Investment description and rationale

- Pan-European diversified fund launched in 2006
- Only 35.4% drawn down to date
- Recent acquisition of a hotel in Barcelona on attractive terms
- Added to CEF I holding in Q1 2010, sourcing €5.6 million of existing units at 21% discount to September 2009 valuation
- Forecast IRR of around 17% over the life of the fund

Pullman Barcelona Skipper

Recent events and outlook:

- Unlikely this deal could be replicated in current market

Please refer to Important Information regarding forecasts

Source: Schroders, March 2010

CEF I: portfolio holdings

Pradera Central & Eastern Fund

Investment description and rationale

- Provides exposure to 8 shopping centres primarily in Poland and Czech Republic valued at €247 million
- High initial yield of underlying assets
- Specialist manager with good track record
- Set up costs and property acquisition expenses already written off
- Projected IRR of 15% using conservative assumptions over remaining 6 year life

Galeria Gniezno Shopping Center, Gniezno, Poland

Recent events and outlook:

- Poland and Czech Republic among our most favoured markets with high economic growth and consumer spending forecasts

Please refer to Important Information regarding forecasts

Source: Schroders, March 2010

Schroders

Important information

Participation in the Schroder Property multi-manager service may involve investment in various asset classes including property equity and collective investment schemes (“Funds”) within the meaning of Section 235 of the Financial Services and Markets Act 2000 (“FSMA”). Most of these Funds are not authorised unit trust schemes, OEICs or recognised schemes within the meaning of the FSMA and therefore constitute unregulated collective investment schemes.

Investors and potential investors should be aware that past performance is not a guide to future returns. No warranty is given, in whole or in part, regarding performance of the portfolio and there is no guarantee that the investment objectives will be achieved. The value of units and other investments and the income from them may fluctuate upwards or downwards and cannot be guaranteed. Property-based pooled vehicles such as property unit trusts, invest in real property, the value of which is generally a matter of a valuer's opinion. It may be difficult to deal in the units or to sell them at a reasonable price, thus creating a liquidity risk. There may be no recognised market for units in the Funds and, as a result, reliable information about the value of units in the Funds or the extent of the risks to which they are exposed may not be readily available. A potential conflict with the Manager’s duty to the client may arise where the Manager invests in units in a Fund(s) managed by itself or an Associate. However the Manager will ensure that such transactions are effected on terms which are not materially less favourable than if the potential conflict had not existed.

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Schroders

Currency Mandate

Performance Review

for

Shetland Islands Pension Fund

25th May 2010

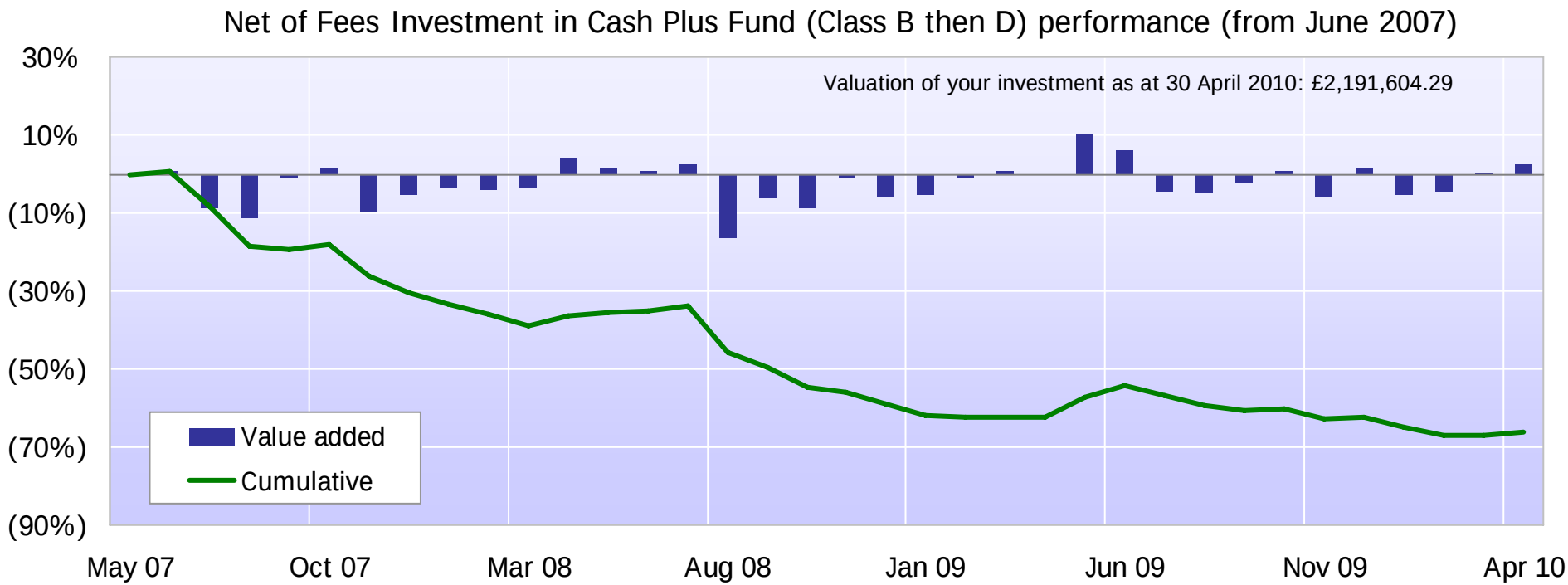
Agenda

- Active mandate specification and objectives
- Performance review
- Recent market events: impact on performance
- Update on Record
- Appendix

Currency mandate specification

- Fund: Record Currency Alpha – Cash Plus
  (7 times geared currency strategy)
- Inception: 26th June 2007
  - Switched from Unit Class B to D (1st April 2009)
- Investment size: £ 5,000,000
- Investment objectives:
  - Expected annual currency return of 21% plus £ interest
  - Expected tracking error 30% p.a.
  - Currency Universe : USD, EUR, GBP, CHF, JPY, AUD, CAD, NZD, NOK, SEK, SGD

Shetland Islands track record



As at 30th April 2010	Fund	Benchmark	Currency return	Degeared return
Last 12 months	(6.77%)	0.48%	(7.25%)	(1.04%)
Since inception (Jun-07)	(25.17%) p.a.	3.36% p.a.	(28.53%) p.a.	(4.08%) p.a.

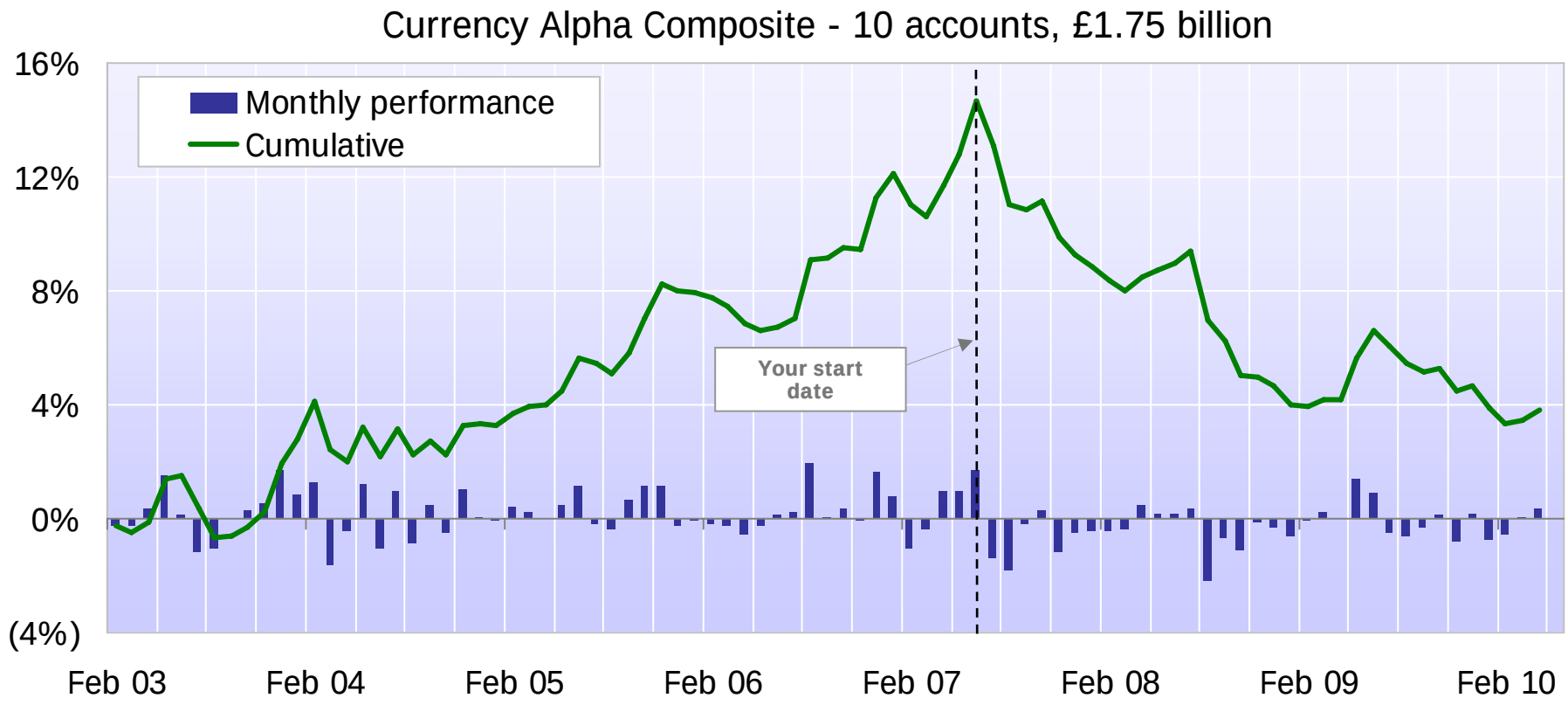
Source: Record Currency Management

Your active track record (net of fees)

As at 30th April 2010	Fund	Benchmark	Currency return	Degeared return
Month	2.25%	0.04%	2.21%	0.32%
Last 3 months	(2.11%)	0.11%	(2.21%)	(0.32%)
Calendar Year to Date	(7.47%)	0.14%	(7.61%)	(1.09%)
Last 12 months	(6.77%)	0.48%	(7.25%)	(1.04%)
Since inception (Jun-07)	(25.17%) p.a.	3.36% p.a.	(28.53%) p.a.	(4.08%) p.a.

Source: Record Currency Management

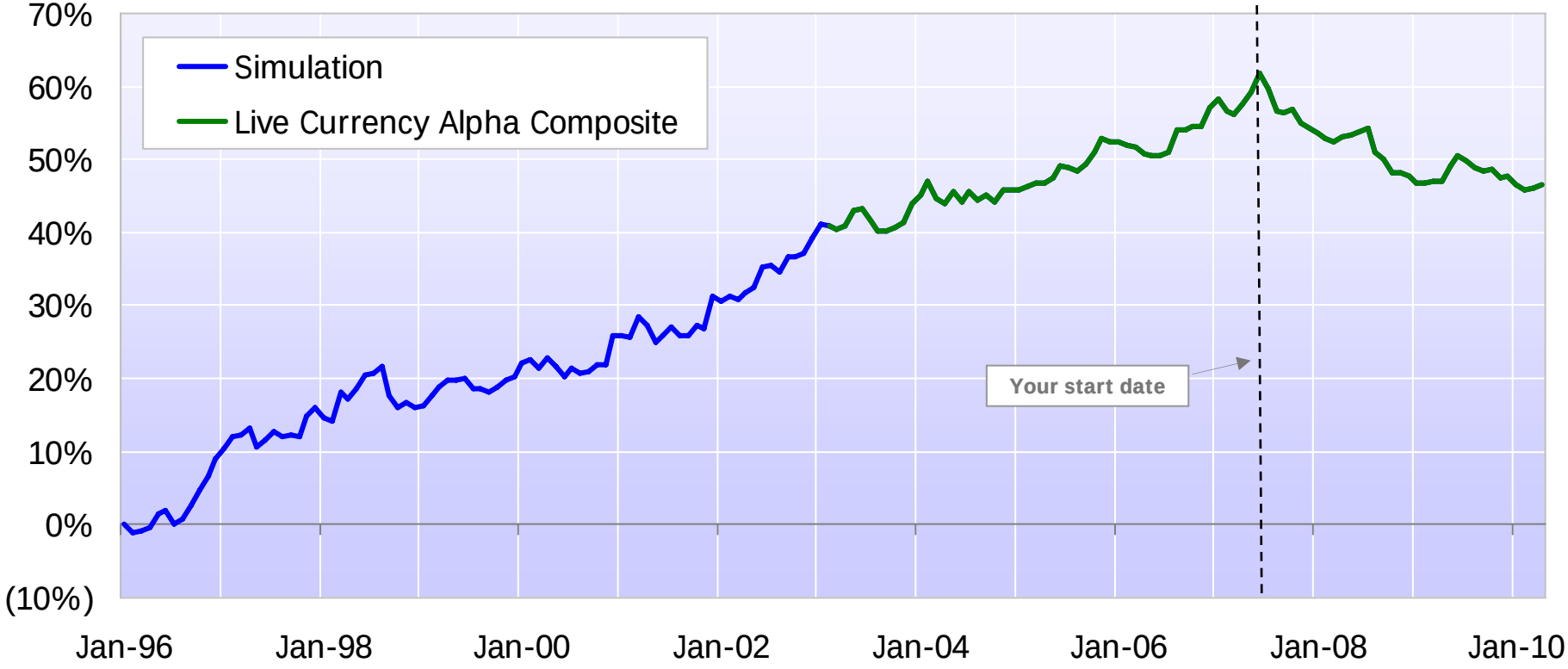
Seven-year live track record



As at 30th April 2010	Value added	Tracking Error	Information Ratio
Since inception (Feb-03)	0.51% p.a.	2.84% p.a.	0.18

Source: Record Currency Management. Returns of all clients in the composite are weighted in US dollars and scaled to a gearing ratio of one. The volatility of returns will be greater if higher leverage is applied. Client numbers and assets are correct as at 30th April 2010

Longer term performance



As at 30th April 2010	Value added	Tracking Error	Information Ratio
Entire period (Feb-92)	2.22% p.a.	3.75%	0.59

Source: Record Currency Management. Simulated returns are for information only

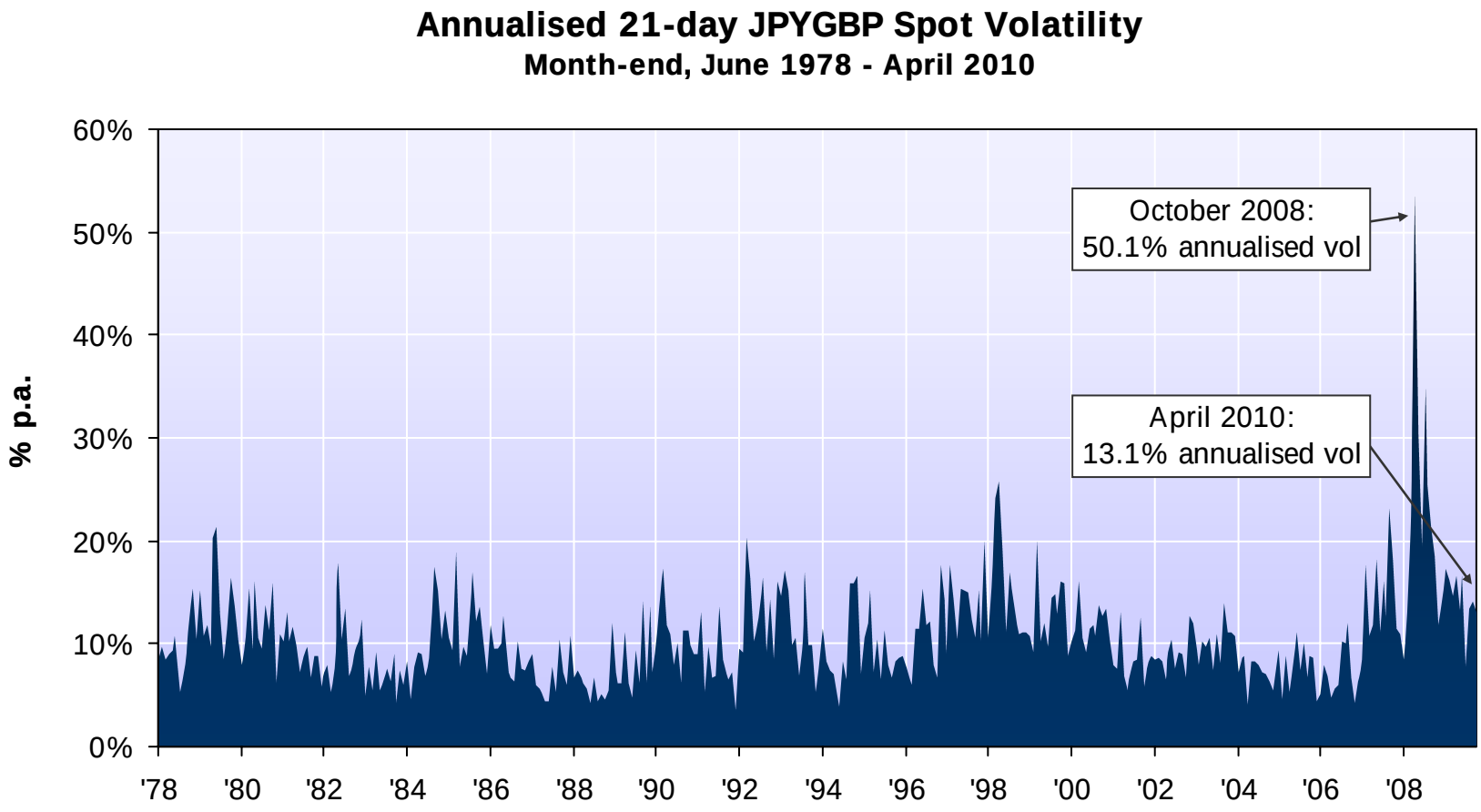
Commentary – 2009/2010

- Q3 2009 risk appetite fluctuated due to conflicting economic data preventing high interest rate currencies from maintaining their positive momentum - in combination with the heightened market volatility this caused losses in the Trend/FRB module

- Q4 2009 was again the subject of mixed news. Risk aversion however was not the prevalent theme with JPY showing the weakest performance amongst G11 currencies against the notably strong AUD & CAD. Better than expected jobs data from the US saw a recovery by the USD through December. Market volatility affected performance

- Q1 2010 USD and JPY retained safe haven status while EUR and GBP both suffered following bad news. The Greek debt problem saw EUR continue to tumble as a grim outlook for the indebted nation emerged. In the UK, news of positive Q4 GDP growth did little to halt the slide of the Pound whose problems were aggravated with S&P placing a negative outlook on the country and hints to additional quantitative easing by the Treasury. Elsewhere, commodity currencies AUD and CAD appreciated as their economies continued to impress

JPYGBP spot rate volatility



Source: Record Currency Management, WM/Reuters. Annualised volatility of 21 period interval of WM spot rate as at month end

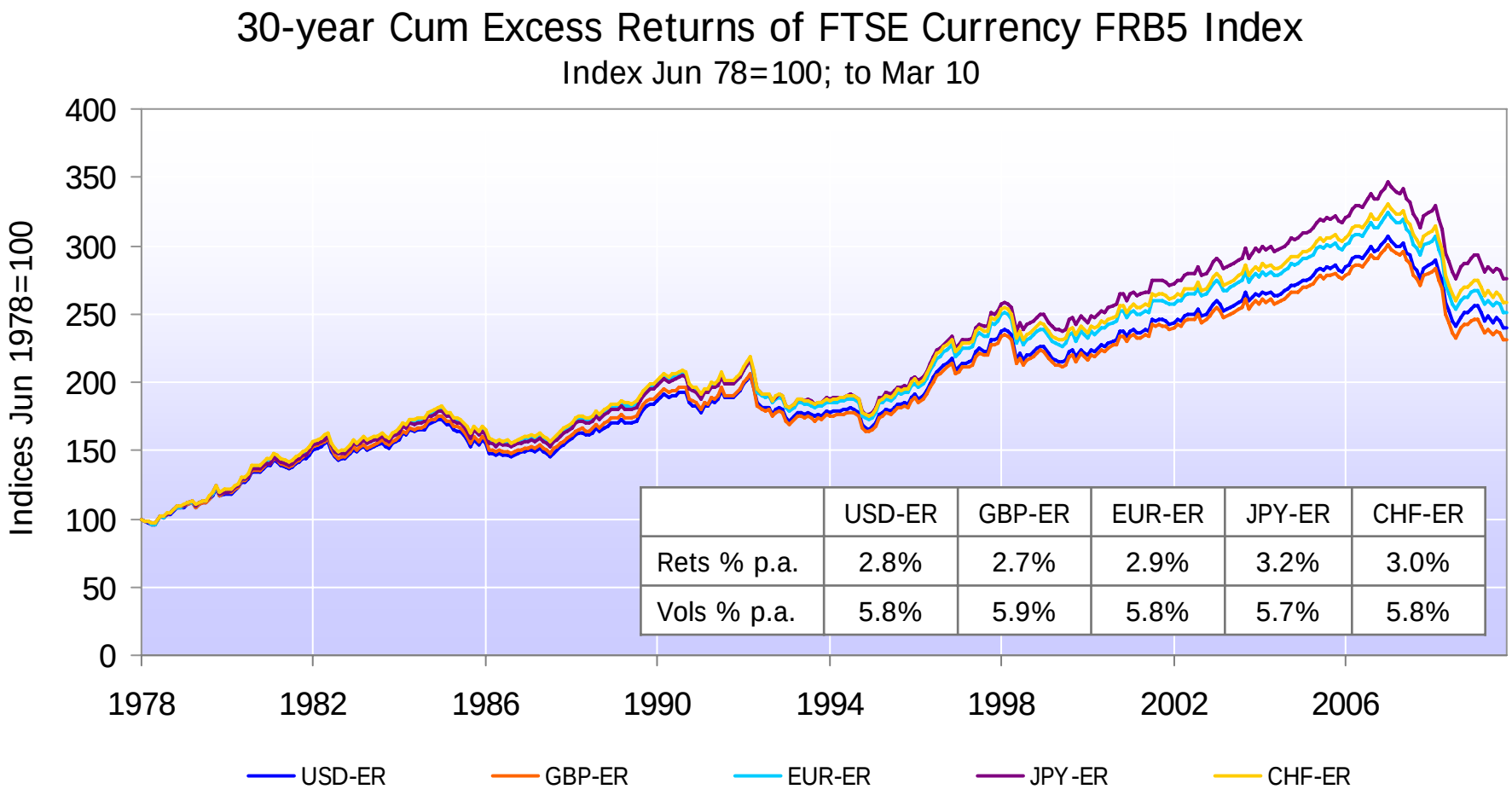
What principles do Record rely on ?

- We believe that:
  - High interest rate (developed) currencies will out-perform in the long term (and low interest rate currencies under-perform)
  - The ‘raw’ volatility of this effect is high, and so we employ a loss-control mechanism, which exploits ‘momentum’ in currencies
- The source of the high interest currencies’ out-performance is *real interest rate differentials*
  - These represent the risk premium paid by deficit country “borrowers” to surplus country “lenders”, and cannot be arbitraged away

Why is the currency FRB a beta ?

- Deficit countries need to continuously find investors to buy and hold their currency (which is a risk)
  - If they fail, their currency falls until they eliminate the deficit
- Surplus countries need to continuously find (risky) currencies to buy with their currency
  - If they fail, their currency rises until they eliminate the surplus
- As long as we have deficit and surplus countries, the deficit countries' currency will have to offer an attractive enough return (for the risk) to encourage buyers
- This is the currency FRB

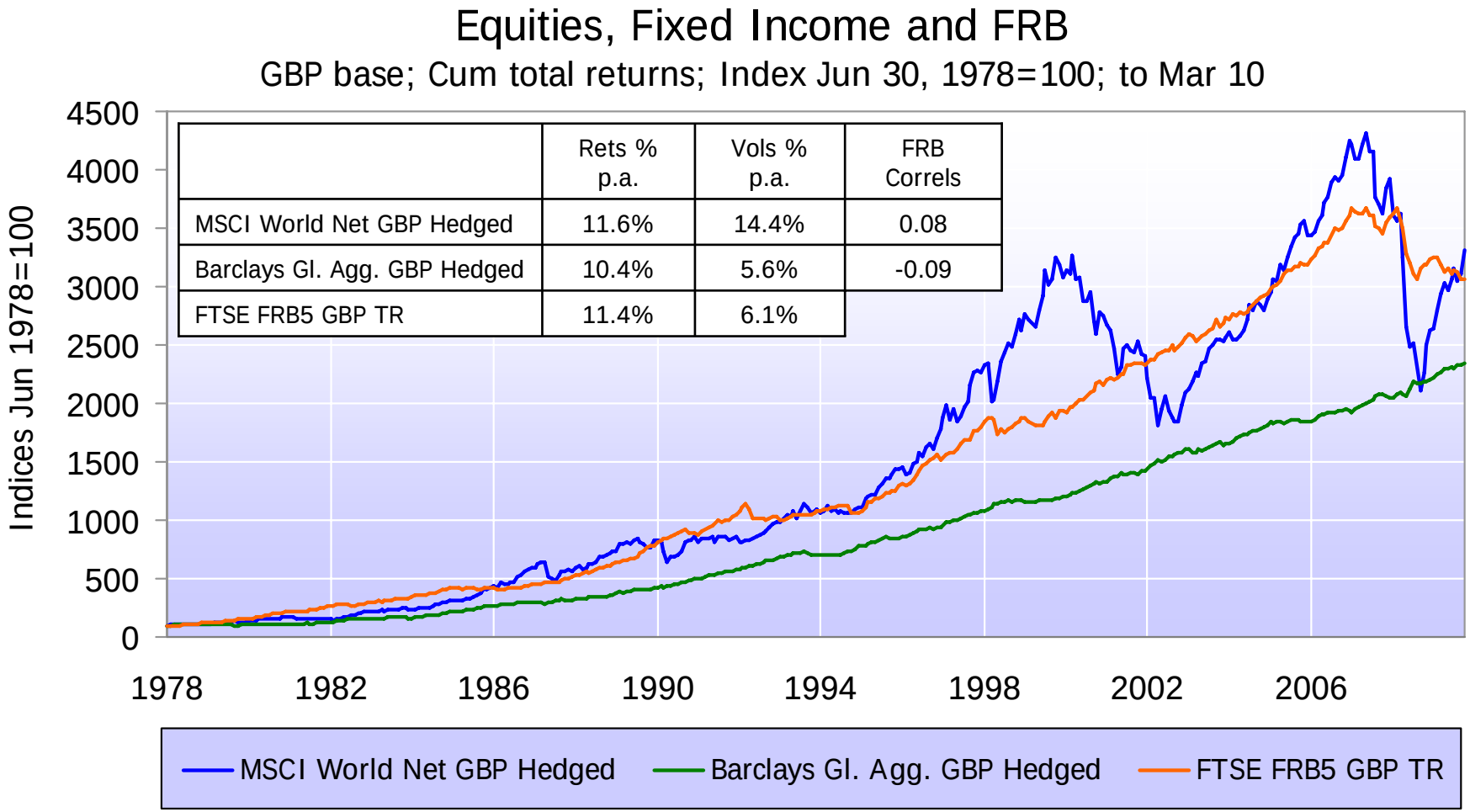
30 year FRB returns



	USD-ER	GBP-ER	EUR-ER	JPY-ER	CHF-ER
Rets % p.a.	2.8%	2.7%	2.9%	3.2%	3.0%
Vols % p.a.	5.8%	5.9%	5.8%	5.7%	5.8%

Source: FTSE Group. Volatility based on monthly returns

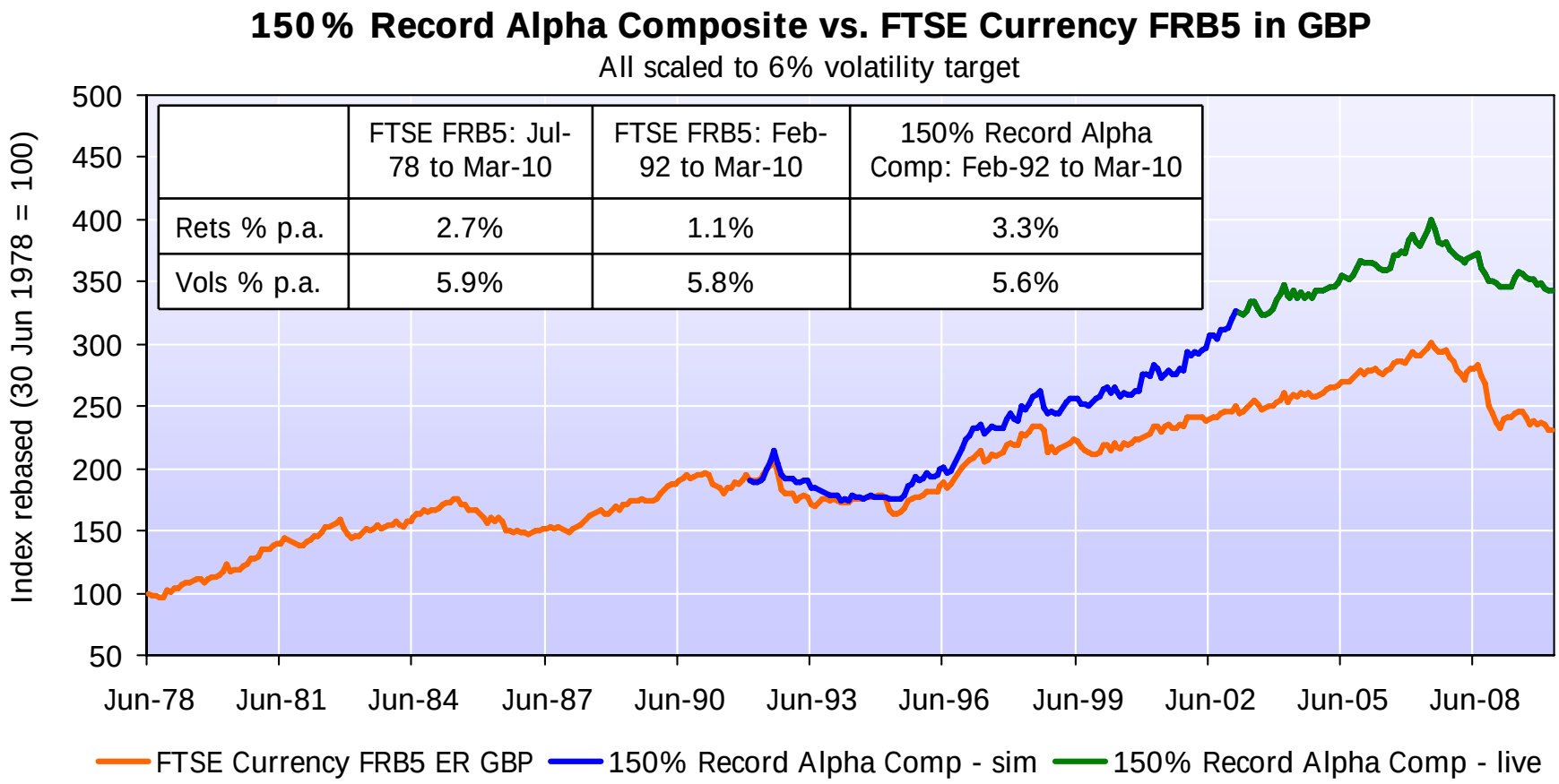
Equities, fixed income and FRB



	Rets % p.a.	Vols % p.a.	FRB Correls
MSCI World Net GBP Hedged	11.6%	14.4%	0.08
Barclays Gl. Agg. GBP Hedged	10.4%	5.6%	-0.09
FTSE FRB5 GBP TR	11.4%	6.1%	

Note: Returns to 31st March 2010. Barclays (ex-Lehman) US Aggregate used as proxy for Lehman Global Aggregate prior to 1990. Hedging based on 1m 'bullet' passive hedging with 100% hedge ratio. Source: Record Currency Management Limited

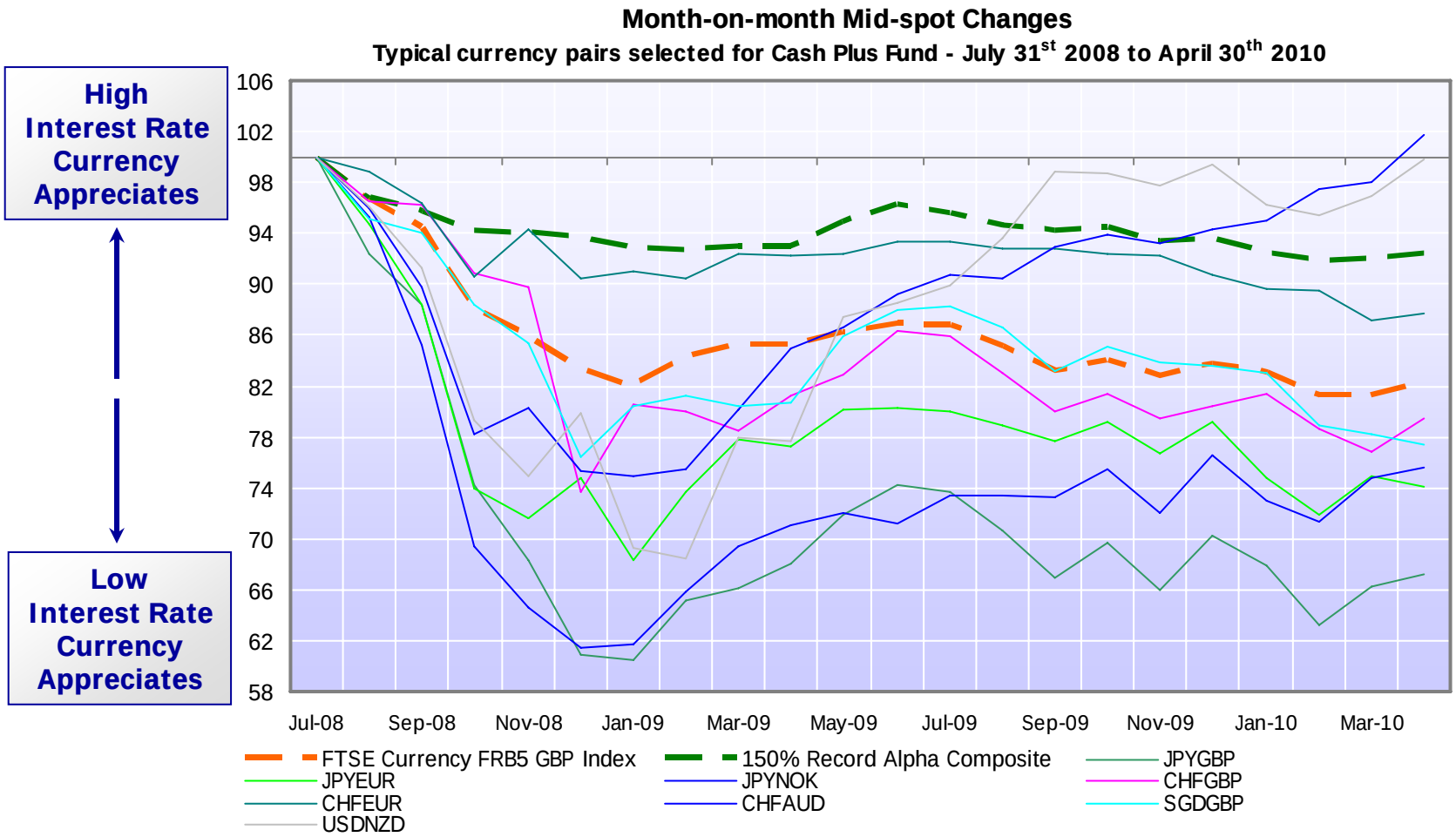
Alpha Composite vs. FRB benchmark



	FTSE FRB5: Jul-78 to Mar-10	FTSE FRB5: Feb-92 to Mar-10	150% Record Alpha Comp: Feb-92 to Mar-10
Rets % p.a.	2.7%	1.1%	3.3%
Vols % p.a.	5.9%	5.8%	5.6%

Note: Returns to 31st March 2010. Volatility based on monthly returns. Source: FTSE Group, Record Currency Management Limited

Alpha Composite vs. FRB benchmark



Performance over period:

Alpha Composite (gearing 150%) (7.6%)

FTSE FRB5 GBP Index (gearing 100%) (17.6%)

Source: Record Currency Management, FTSE Group

Outlook

We do not believe that the current low interest rate environment undermines the long-term prospects for FRB

- Historical correlation between the size of annual FRB returns and the size of interest rate differentials is not strong
- Spot rate movements contribute a significant proportion of the total FRB returns. Spot rates tend to respond to the tightening or loosening of monetary policy and reinforce the interest rate differential signal
- We believe interest rate differentials are driven by fundamental differences between economies, and that the degree of global harmonisation required to erode these differences is unlikely

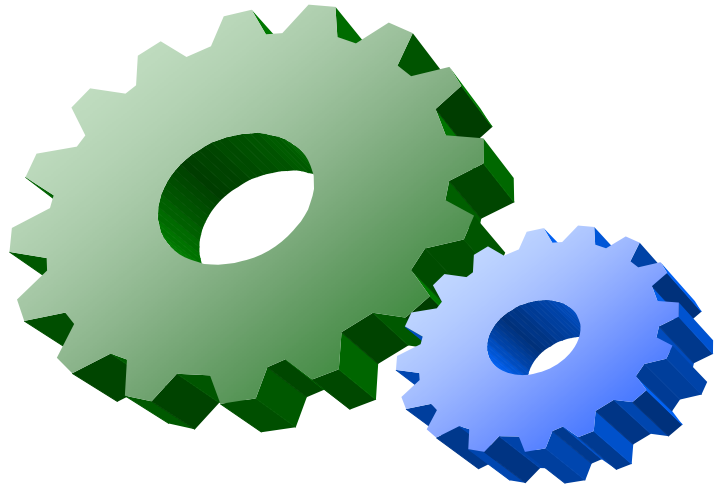
Two systematic processes

Diversification and Systematic Risk Controls

Two independent investment processes

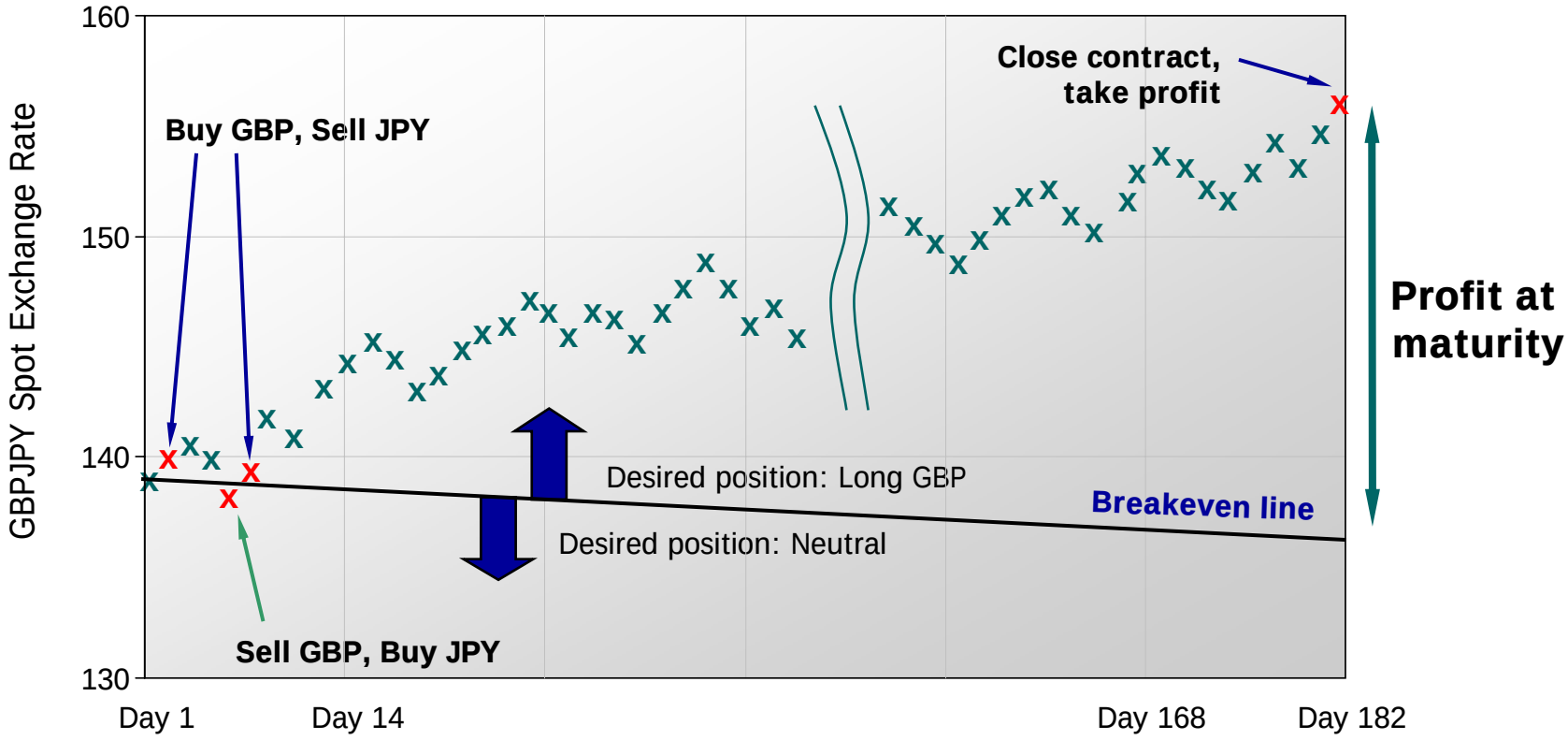
- **TREND / FORWARD RATE BIAS**
  - 5/6th of programme
  - Substantial value added
- **RANGE TRADING**
  - 1/6th of programme
  - Overall volatility reduction

More stable return pattern



One component of the 48

If the £ strengthens vs. the ¥, the process allows profits to run



Note: The manager observes the prices periodically and systematically closes positions below the breakeven line at the point of observation. Profits will be reduced by the associated trading costs

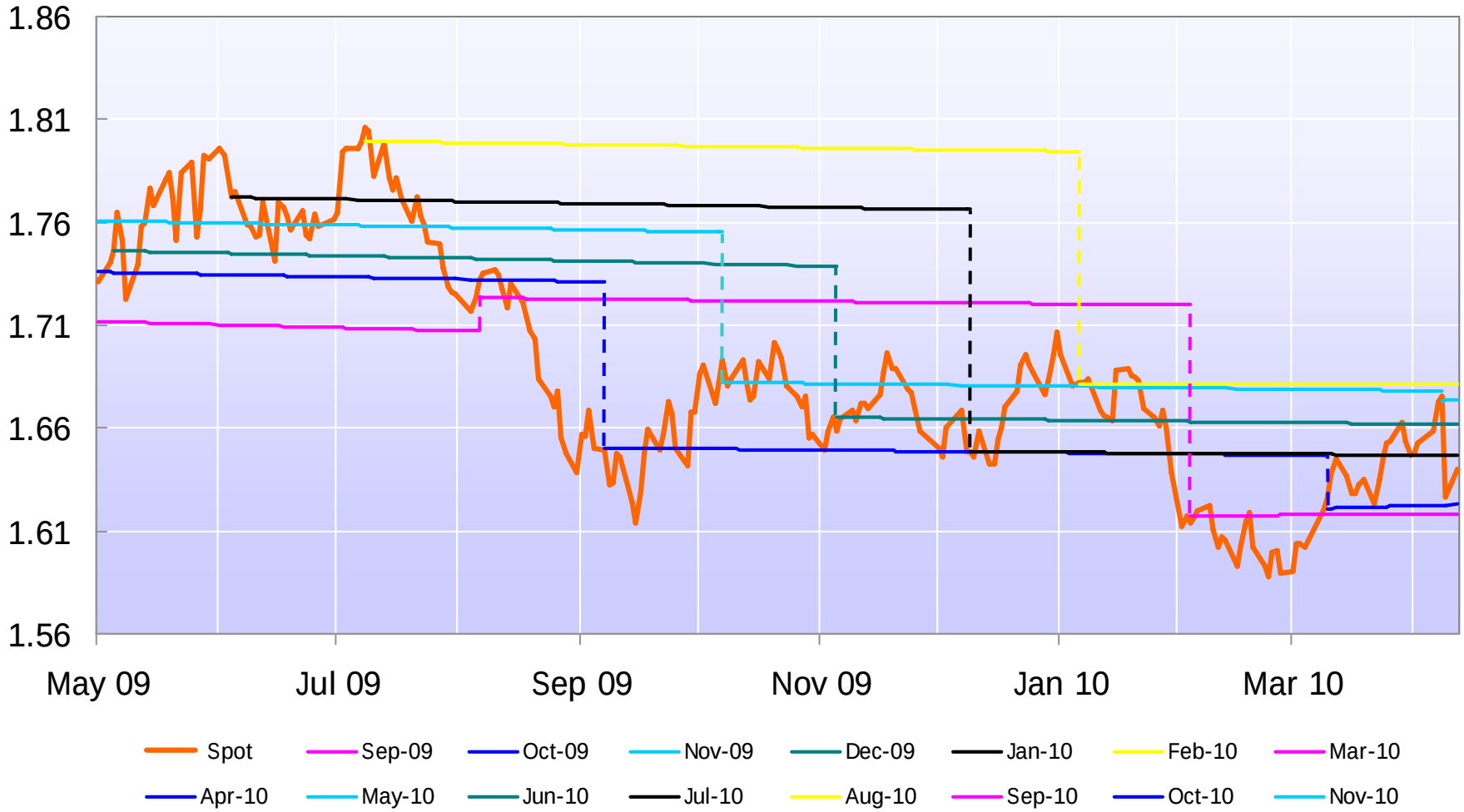
Currency pair selection

Trend / FRB				Range Trading			
Jan	Feb	Mar	April	Jan	Feb	Mar	April
CHFEUR	CHFEUR	CHFEUR	CHFEUR	---	NZDAUD	NZDAUD	NZDAUD
CHFGBP	CHFGBP	CHFGBP	CHFGBP	---	NOKCAD	NOKCAD	NOKCAD
USDEUR	USDEUR	USDEUR	JPYEUR	---	---	SGDCHF	SGDCHF
USDGBP	USDGBP	USDGBP	JPYGBP	---	---	CADUSD	CADUSD
JPYAUD	JPYAUD	JPYAUD	USDAUD	---	---	---	---
USDNZD	USDNZD	USDNZD	JPYNZD	---	---	---	---
CHFNOK	CHFNOK	CHFNOK	CHFNOK	---	---	---	---
---	---	CADEUR	CADEUR	---	---	---	---

denotes **SHORT** currency position
denotes **LONG** currency position

Source: Record Currency Management, new currency pairs selected for inclusion in Cash Plus Fund T101 in the four months dates to April 2010. Trend/FRB positions shown for Cash Plus Fund T101 are one of multiple monthly pair selections made for the Cash Plus Fund and other pair selections may differ from that shown. Range Trading selections shown across multiple buckets and exposure may not be equally weighted.

GBPCHF positions



Source: Record Currency Management, based on Cash Plus Fund T101 from 29 May 2009 to 10 May 2010.

Update on Record

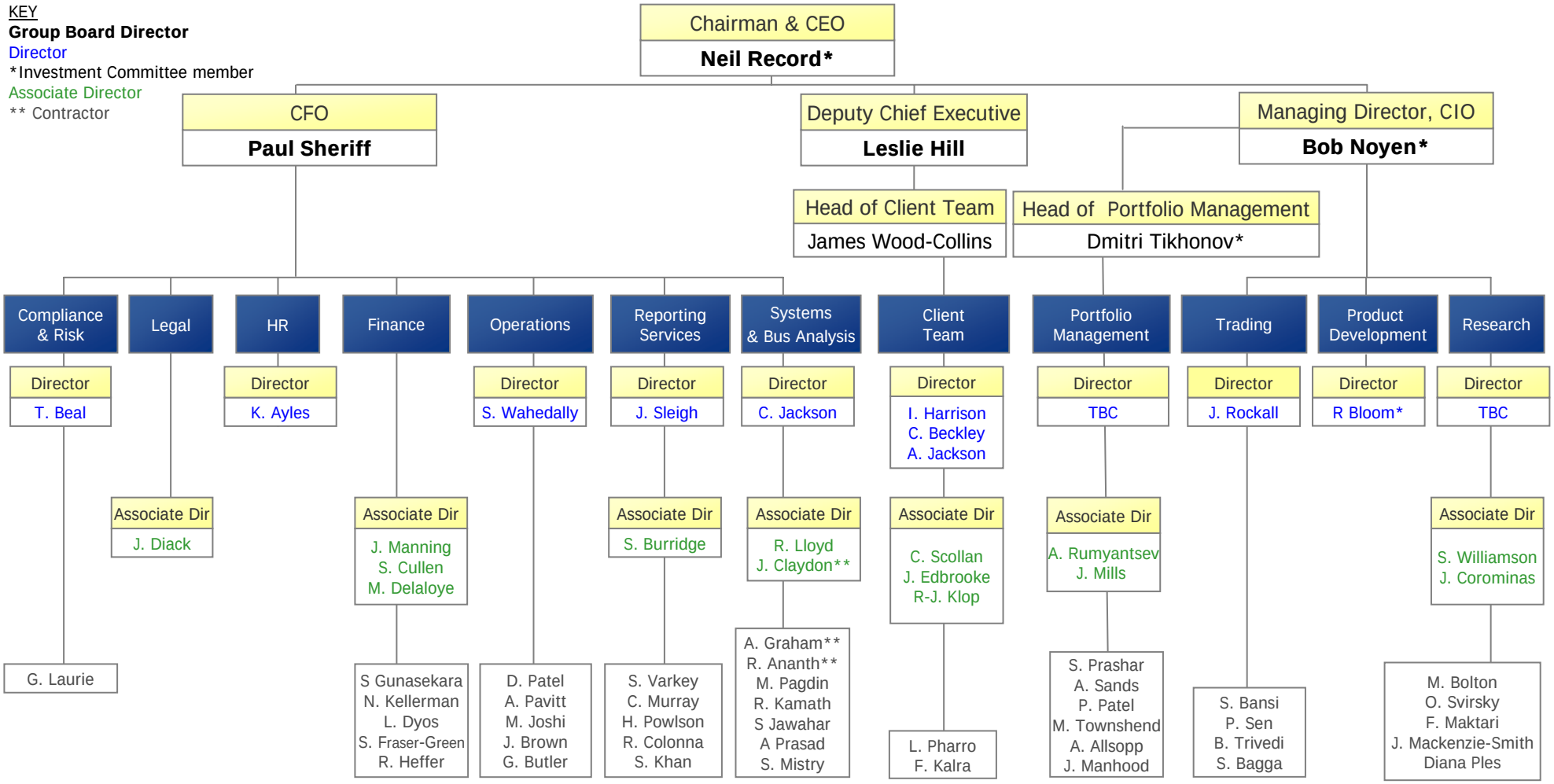
- AUM: £22.4bn as at 31st March 2010
- Total Staff: 69 people *(incl 2 contractors)*
- Staff gains (Q4 2009-Q1 2010)

Name	Role	Start Date	Previous Employer
Julien Manhood	Product Specialist - Portfolio Management	Oct-2009	Graduate Recruit
Sanjiv Mistry	Support Analyst	Nov-2009	Cube Technology
James McKenzie-Smith	Investment Researcher	Dec 2009	Ernst & Young
Sarah Burridge	Reporting Services Manager	March 2010	Lloyds TSB
Sara Gunasekara	Management Accountant	March 2010	Graduate Accountant

- Staff losses (Q4 2009-Q1 2010)

Name	Role	Start Date	Previous Employer
Elena Gould	Settlements	Dec 2009	ICE in London
Pam Beasley	Receptionist	Dec 2009	Retired
Dave Murphy	Head of Research	Dec 2009	Retired
Yianni Doumenis	Client Team	March 2010	--

Organisation structure



Credit control

- Minimum long-term credit rating of A1/A+
- Regularly review counterparties
- Equity and credit default swap prices and rating agencies' outlook on credit ratings
- 'Excess' margin from investment bank prime brokers removed
- Increased credit diversification of cash deposit portfolios

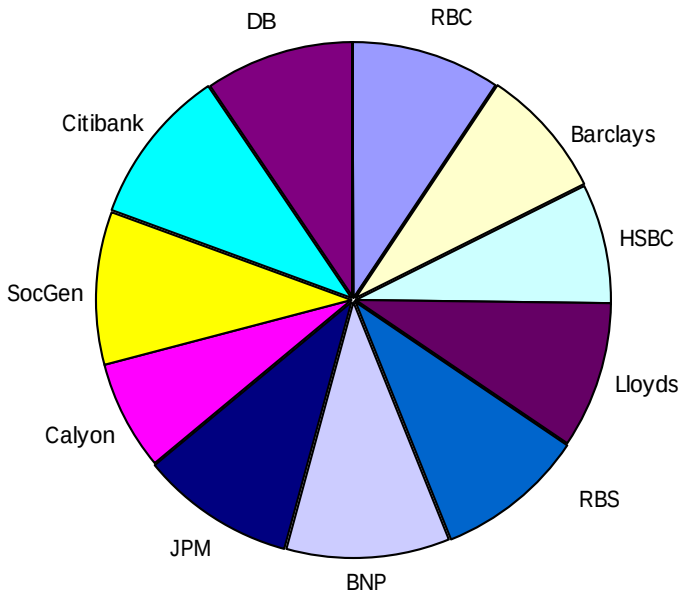
Prime Broker: RBS and DB

(i) the initial margin

(ii) any excess margin above MTM that we have left there (as low as practicable)

(iii) any other time deposits

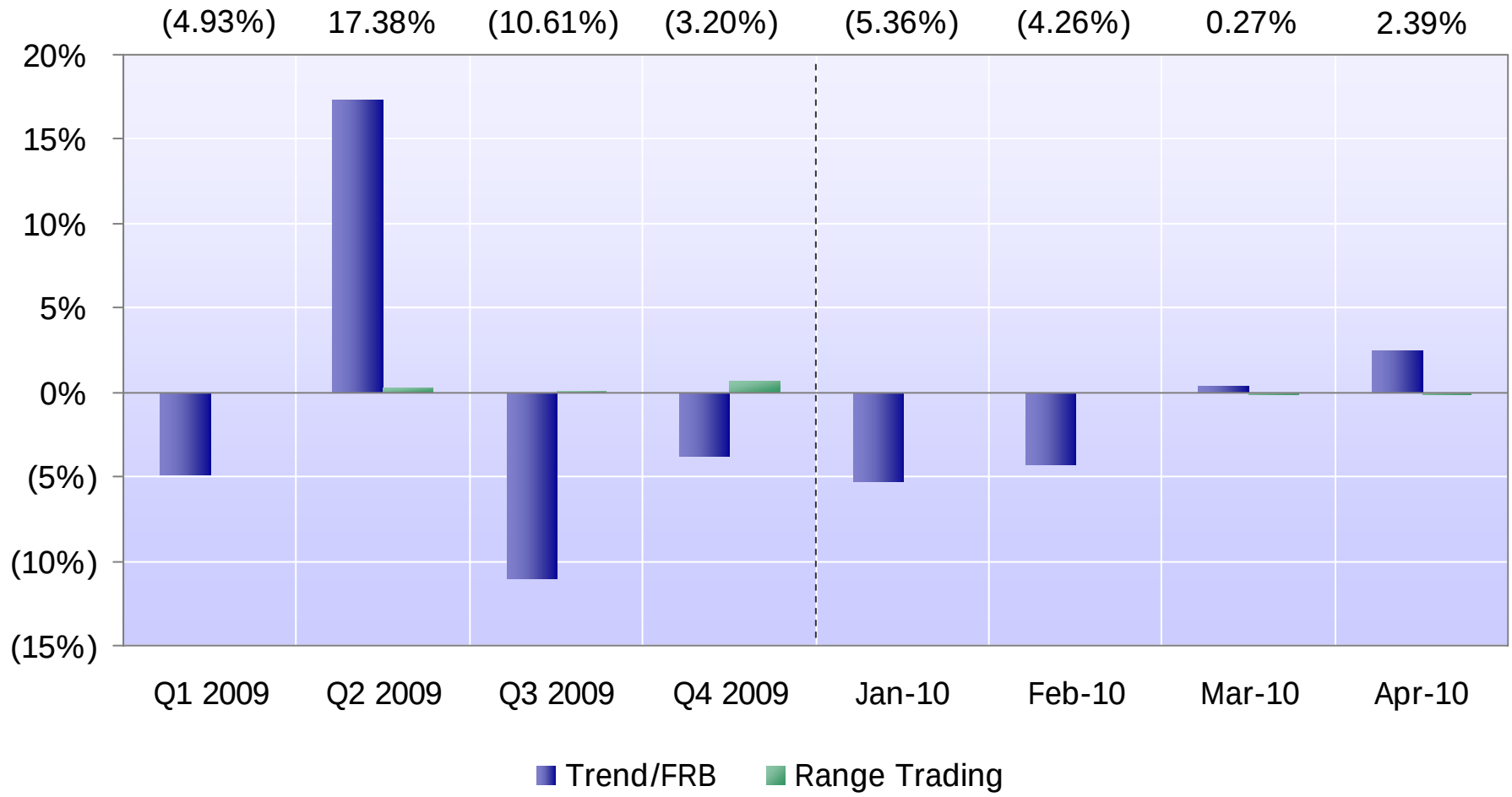
Cash Plus Exposure
As at 30th April 2010 (% of NAV)



- Note exposure to Northern Trust excluded as less than £10K

Appendix

Cash Plus performance attribution



Note: attribution is done on the basis of Cash Plus – Class A currency returns. Trend/FRB, Range Trading attribution is estimated.

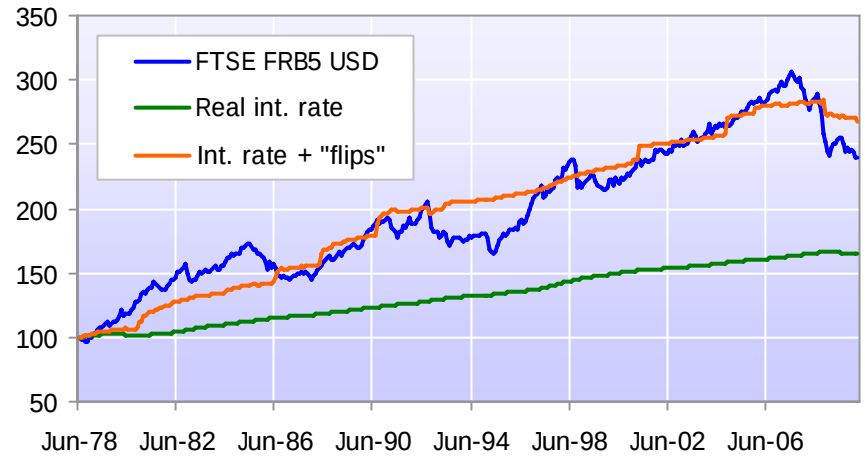
How is the currency FRB manifested ?

The tendency of high interest rate currencies' "return" to outperform low interest rate currencies

- "Return" is the interest rate plus/minus currency appreciation/depreciation (versus the other currency)
- In our observation:
  - Nominal interest rate differentials largely reflect real (i.e. after-inflation) interest rate differentials
  - High real-interest-rate currencies outperform low real-interest-rate currencies by at least the extent of the real interest rate differential in the long-term

How is the return generated ?

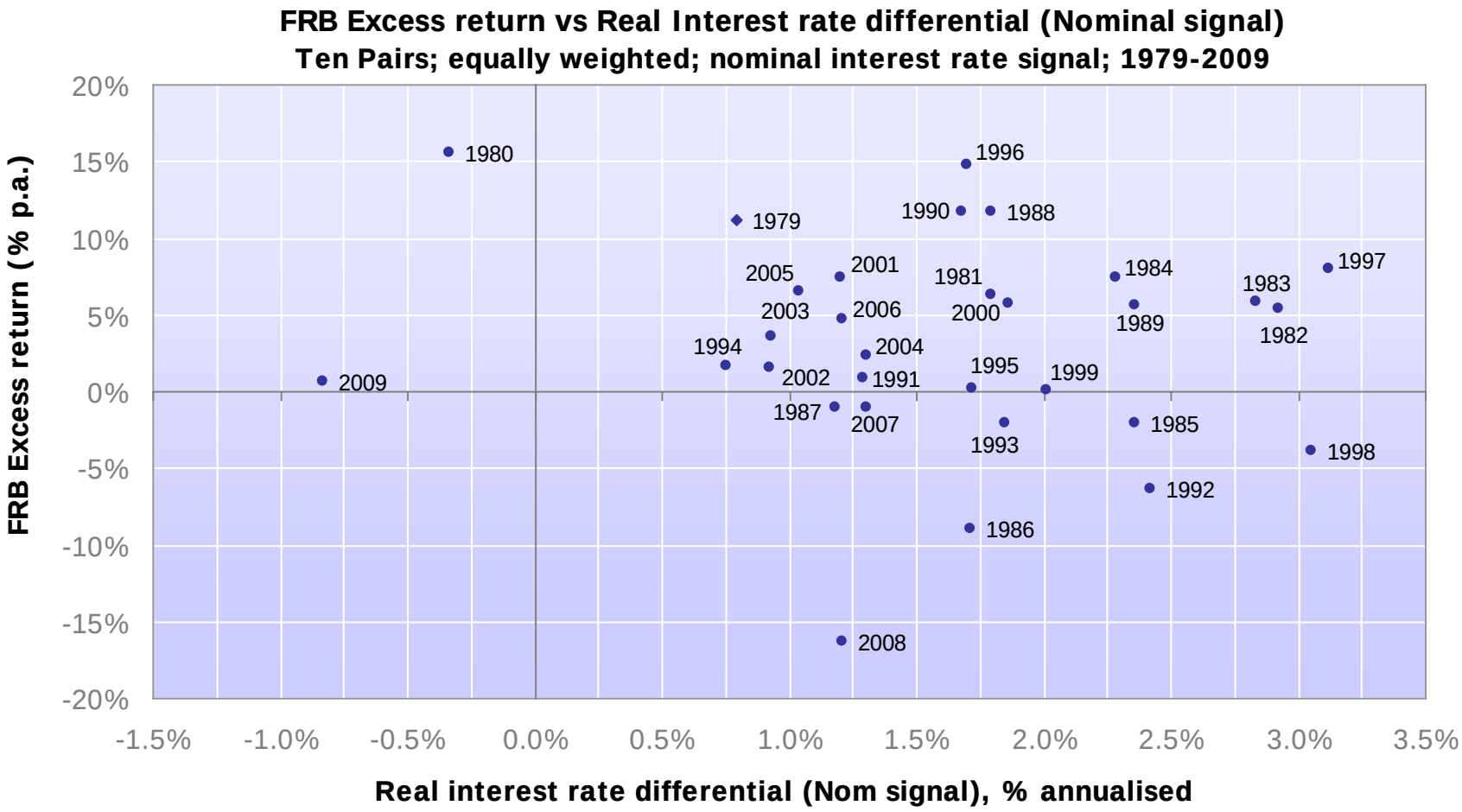
- FRB strategy can collect real interest rate differentials, based on nominal interest rate signals
  - Long higher interest rate currency vs. lower
  - Real and nominal interest rate differentials highly correlated



- Over time, this accounts for only about half the observed “FRB beta” return
- The other half is derived from real spot appreciation of the higher rate currency
  - Currency valuations can be stretched far from long-term means
- In compressed interest rate differential environments, the FRB return is particularly driven by real spot rate appreciation

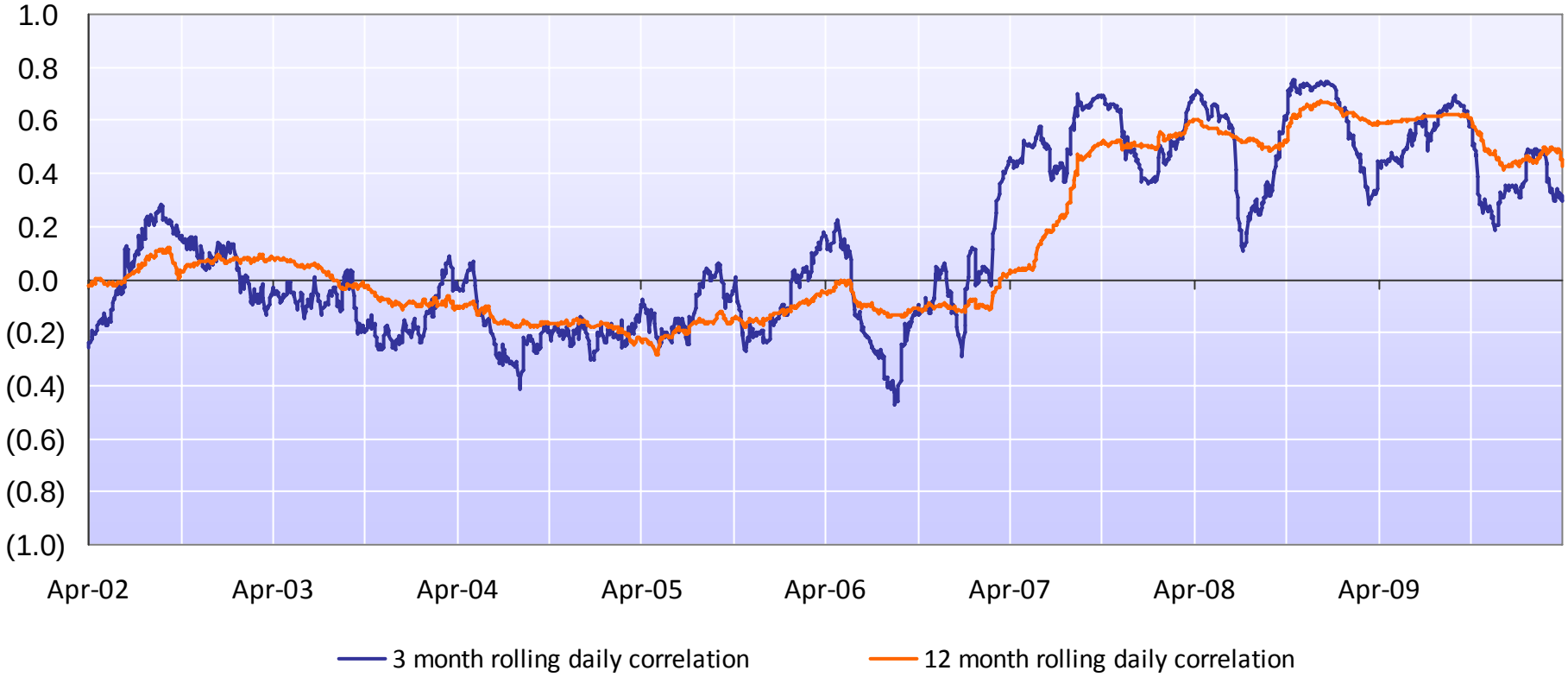
FTSE Currency FRB5 USD excess return index compared to real interest rate differential, with direction of interest rate differential based on nominal rate signal, to Mar-10.
Source: Record Currency Management

Real interest rate differentials



Source: Record Currency Management

Correlation of FTSE 100 and JPYGBP



	2002	2003	2004	2005	2006	2007	2008	2009	2010 YTD
Annual correlation	0.06	(0.09)	(0.17)	(0.13)	(0.12)	**0.50**	**0.66**	**0.44**	**0.34**

Source: Record Currency Management, Bloomberg. Based on daily observations. Correlations calculated to 1st April 2010.

Risk warnings

All data, unless otherwise stated in the footnote of the relevant page is as at 11th May 2010.

This material is provided for informational purposes only and is not intended to reflect a current or past recommendation, investment advice of any kind, or a solicitation of an offer to buy or sell any securities, Record Currency Management Ltd products or investment services.
The views about the methodology, investment strategy and its benefits are those held by Record Currency Management Limited. There is no guarantee that any of the strategies and techniques will lead to superior investment performance. All beliefs based on statistical observation must be viewed in the context that past performance is no guide to the future. There is no guarantee that the manager will be able to meet return objectives and tracking error targets.
The investment process described represents the views of the manager and is true at the time of writing and is subject to change without notice.

Fund only risk warning
Applications for shares of the funds can only be made on the basis of the current prospectus of the Record Umbrella Fund, an Irish-domicile, non UCITS Qualifying Investor Unit Trust, together with the latest audited annual report (and, if published, subsequent semi-annual report). Please read the prospectus carefully prior to investing. It is the responsibility of any persons in possession of this document and any persons wishing to make applications for shares pursuant to the prospectus to inform themselves of, and to observe, all applicable laws and regulations of any relevant jurisdictions. In certain jurisdictions, shares may not be available, publicly and/or otherwise, for purchase and the distribution of this document may be restricted.

Performance warnings
Past performance is not a guarantee of future results. Portfolio returns are gross of fees and assume the reinvestment of all returns. The investment return and principal value of an investment will fluctuate so that when realised, may be worth more or less than the original investment.
This presentation shows portfolio returns on an unleveraged basis. Any increase of the gearing ratio will lead to greater volatility of the investment and potentially greater losses.
Investors with significant leverage must be aware of the risk involved in the investment proposed and of the fact inherent in such investments is the potential to lose all of the sum invested.
The absolute return product often will have high levels of exposure, up to 50% of the total commitment (long or short position), to a single currency therefore investors must be aware that significant losses may be realised in a short period of time due to sudden changes in relative currency values.
Changes in rates of exchange between currencies will cause the value of investments to decrease or increase.
The views contained herein are as of 11th May 2010 and may have changed since that time.
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> Shetland Islands Council Pension Fund

Pages 6-21

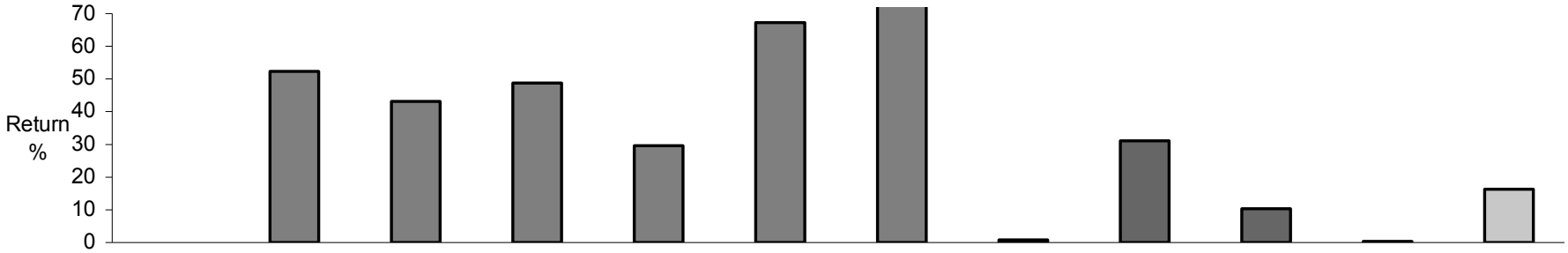
Shetland Islands Council Capital and Miscellaneous Funds

Pages 23-51

Date: **May 25th 2010**
By: **Karen Thrumble**

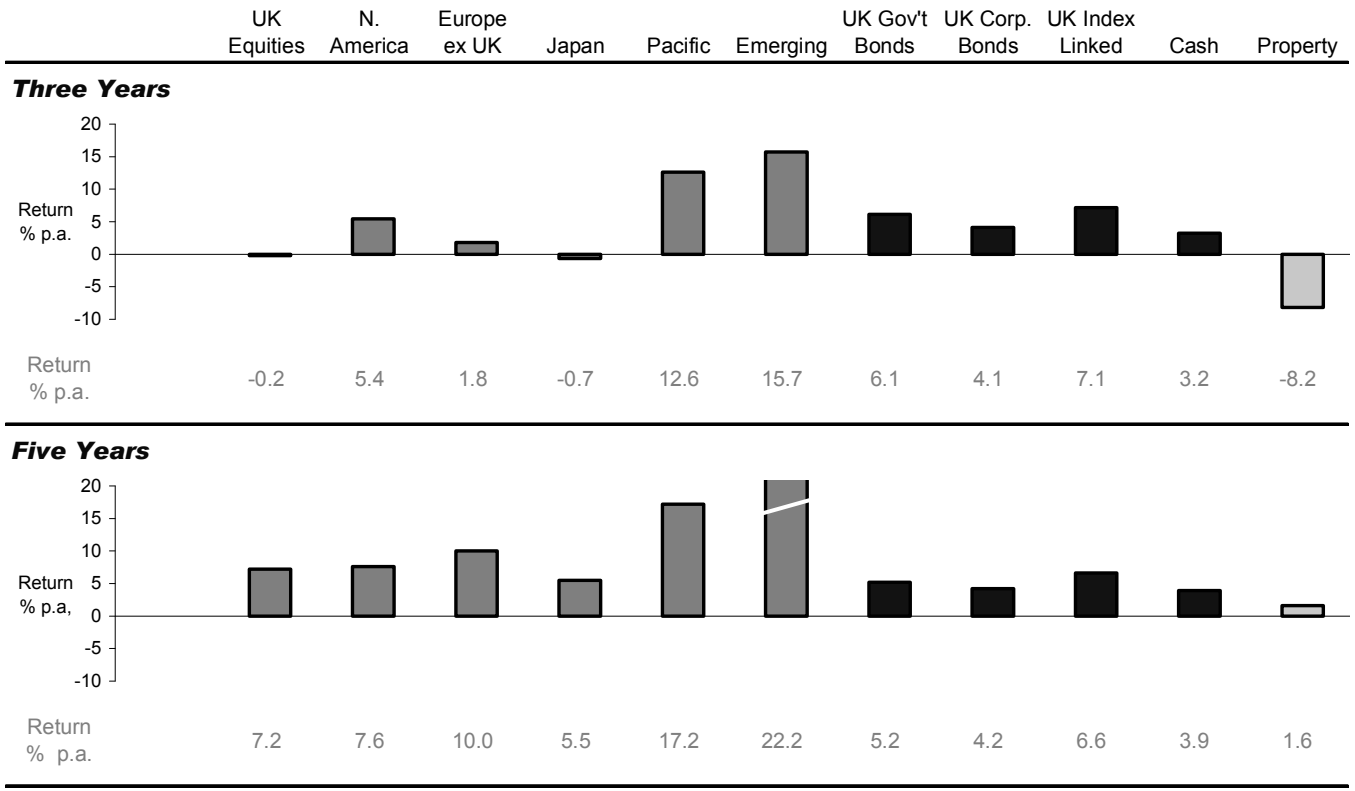
SECTION 1
Market Background

Year to March 2010



	UK Equities	N. America	Europe ex UK	Japan	Pacific	Emerging	UK Gov't Bonds	UK Corp. Bonds	UK Index Linked	Cash	Property
Return %	52.3	43.2	48.8	29.6	67.2	74.5	0.8	31.1	10.3	0.4	16.3

Longer Term


UK Equities
N. America
Europe ex UK
Japan
Pacific
Emerging
UK Gov't Bonds
UK Corp. Bonds
UK Index Linked
Cash
Property
Three Years
Return % p.a.
20
15
10
5
0
-5
-10
Return % p.a.
-0.2
5.4
1.8
-0.7
12.6
15.7
6.1
4.1
7.1
3.2
-8.2
Five Years
Return % p.a,
20
15
10
5
0
-5
-10
Return % p.a.
7.2
7.6
10.0
5.5
17.2
22.2
5.2
4.2
6.6
3.9
1.6

SECTION 2
Total Pension Fund Performance

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> Shetland Islands Council Pension Fund

Fund Structure And Value

Values £'000	Mandate	Value at 31/03/2009	% Fund	Value at 31/03/2010	% Fund
BLACKROCK	Multi Asset	135,803	92	204,313	92
SCHRODERS	Property	9,134	6	15,621	7
RECORD	Active Currency	2,354	2	2,143	1
Total Fund		147,291	100	222,078	100

Fund Benchmarks

	Blackrock	Schroders	Record	Total	Index
UK Equities	42.9			37.5	FTSE All Share
North America	9.9			8.7	MSCI North America NDR
Europe ex UK	14.0			12.2	MSCI Europe ex UK NDR
Japan	9.5			8.3	MSCI Japan NDR
Pacific ex Japan	9.5			8.3	MSCI Pacific ex Japan
UK Bonds	5.0			4.4	FTSE Gilts All Stocks
Corporate Bonds	5.0			4.4	iBoxx £ non Gilts Index
Cash	4.2			3.7	LIBID 7 Day
Property		100.0		10.0	IPD Pooled Property
Currency			100.0	2.5	1 Month LIBOR -0.1%
% of Total Fund B'M	87.5	10.0	2.5	100.0	

PERFORMANCE — LATEST YEAR

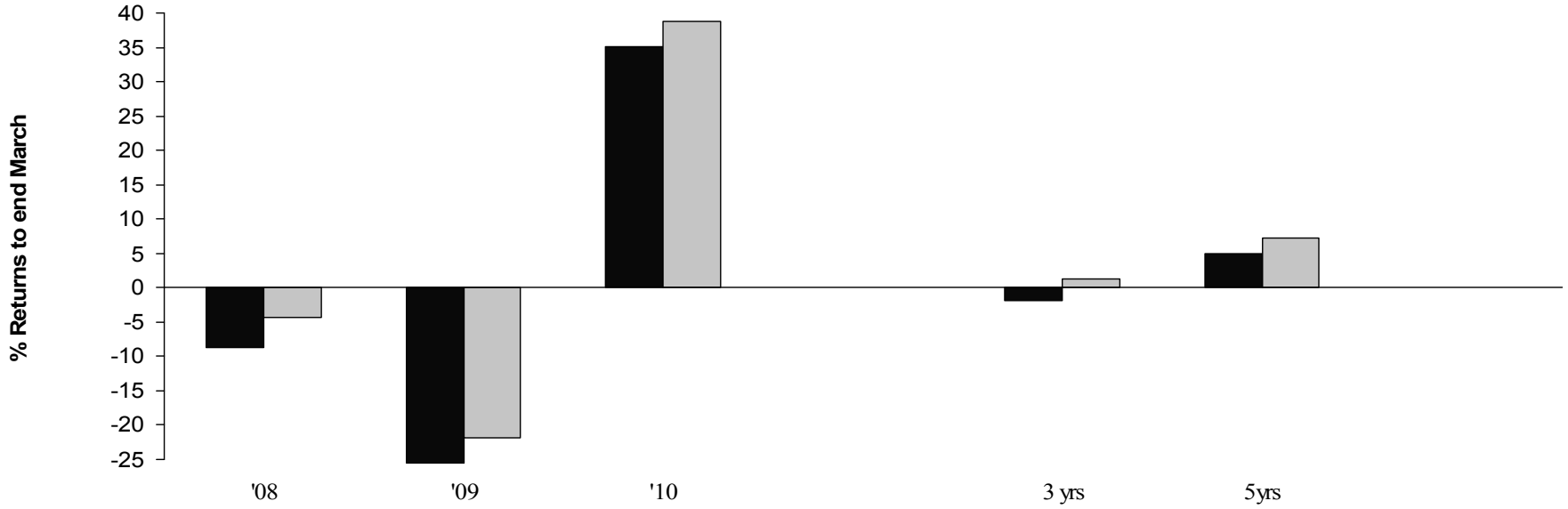
Fund Return		39.7
Benchmark Return		38.8
Relative Performance		0.6
	attributable to:	
	Strategic Allocation	1.2
	Manager Contribution	-0.6

The relative performance can be attributed to the effects of manager contribution and strategic allocation.

Detail

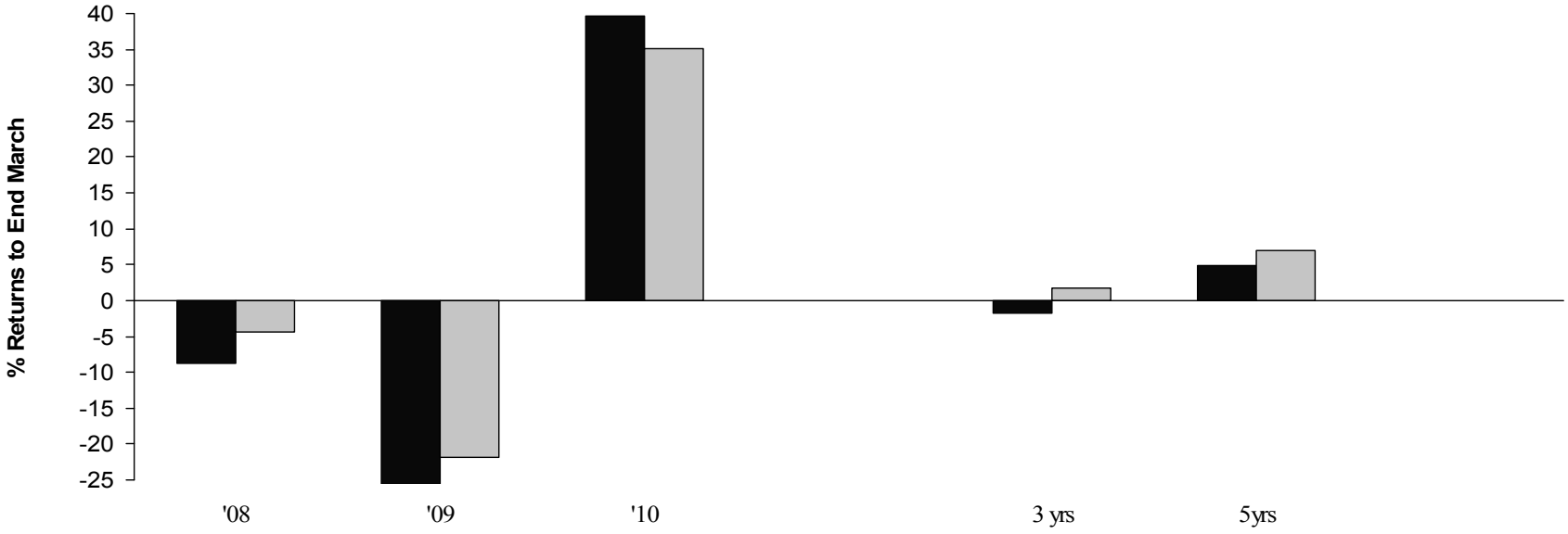
Strategic Allocation				Manager Contribution		
Distribution		Policy	Investment	Weighted	% Return	
Portfolio	Benchmark	Contribution	Manager	Contribution	Portfolio	Benchmark
92.2	87.5	0.2	BLACKROCK	0.3	43.8	43.3
6.2	10.0	0.8	SCHRODER INVEST. MGMT.	-0.8	-2.4	11.6
1.6	2.5	0.3	RECORD CURRENCY MGMT	-0.1	-8.9	0.5
		1.2		-0.6		

Total Fund vs Benchmark Returns



	'08	'09	'10	3 yrs	5yrs
Fund	-8.7	-25.6	39.7	-1.8	4.9
B'M	-4.3	-21.9	38.8	1.2	7.2
Relative	-4.6	-4.8	0.6	-2.9	-2.1

Total Fund vs Local Authority Funds



	'08	'09	'10	3 yrs	5yrs
Fund	-8.7	-25.6	39.7	-1.8	4.9
LA	-2.8	-19.9	35.1	1.7	7.0
Relative	-6.1	-7.1	3.4	-3.4	-2.0
Ranking	100	90	23	100	100

Key Points

Latest Year

> The return of 39.7% was the best the Fund has achieved since measurement began in 1981. This was driven by the rebound of equity markets from the severely depressed levels of the year before.

> For the first time in recent years, performance relative to benchmark was positive. This was primarily due to the low level of property held and the higher than benchmark exposure to equities.

> While Blackrock performed in line with benchmark the active managers disappointed.

Longer Term

> Despite good performance in the latest year the Fund remains well behind its own benchmark over both the three and five years.

> This was mainly due to the poor recent performance of Capital International although Record Currency Management have also detracted from performance, losing almost £3 million since they began management in 2007.

SECTION 3
Blackrock
Multi Asset Portfolio Performance

Quarterly Performance

	---------- 2007 ----------			---------- 2008 ----------				---------- 2009 ----------				2010
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Values (GBPm's)												
Initial							0.0	143.0	135.8	147.3	176.7	182.6
Net Investment							130.2	6.0	-0.0	-0.0	0.7	8.0
Capital Gain/Loss							12.8	-13.3	11.5	29.4	5.3	13.7
Final							143.0	135.8	147.3	176.7	182.6	204.3
Income							0.0	0.0	0.0	0.0	0.0	0.0
Proportion Of Total Fund (%)							92	92	93	92	91	92

Quarterly Returns

Fund	-9.0	8.5	19.9	3.0	7.3
Benchmark	-9.1	8.4	20.0	2.9	7.1
Relative Return	0.1	0.1	-0.1	0.1	0.1

Key Points

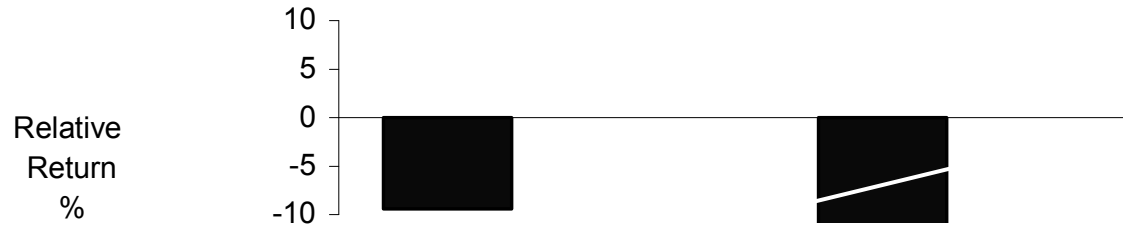
Blackrock was appointed from December 2008 on a multi asset passive basis.

> In the first five quarters of management Blackrock have produced returns broadly in line with the index as would be expected from this style of manager.

> The decision to move passive has had a positive impact on performance as most active managers underperformed the index in the latest year.

SECTION 4
Record Currency Management
Active Currency Portfolio Performance

Performance

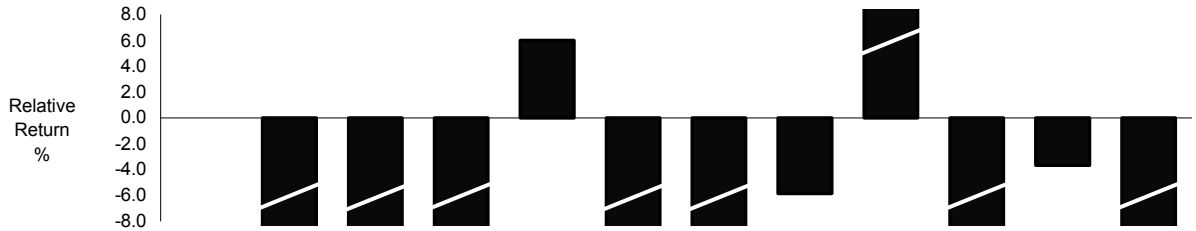


	One Year	From Q2 2007 (% p.a.)
Portfolio	-8.9	-26.6
Benchmark	0.5	3.3
Relative Return	-9.4	-28.9

Quarterly Performance

	---------- 2007 ----------			---------- 2008 ----------				---------- 2009 ----------				2010
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Values (GBPm's)												
Initial	0.0	5.0	4.1	3.6	3.3	3.5	2.9	2.5	2.4	2.8	2.5	2.4
Net Investment	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital Gain/Loss	0.0	-0.9	-0.5	-0.4	0.2	-0.6	-0.4	-0.1	0.4	-0.3	-0.1	-0.2
Final	5.0	4.1	3.6	3.3	3.5	2.9	2.5	2.4	2.8	2.5	2.4	2.1
Income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Proportion Of Total Fund (%)	2	2	2	2	2	2	2	2	2	1	1	1

Quarterly Returns



Fund	-18.4	-11.2	-9.6	7.4	-18.2	-13.8	-5.6	17.2	-10.9	-3.6	-9.5
Benchmark	1.5	1.6	1.4	1.4	1.4	1.0	0.3	0.2	0.1	0.1	0.1
Relative Return	-19.6	-12.6	-10.8	6.0	-19.3	-14.7	-5.9	17.0	-11.0	-3.7	-9.6

Key Points

Latest Year

> In the latest year the portfolio has fallen in value from £2.4m to £2.1m with a return of -8.9%.

> This return was 9.4% below the benchmark.

Longer Term

> In the eleven full quarters that the portfolio has been in operation it has fallen in value from £5m to £2.1m with a return of -26.6%pa.

> Although disappointing this is not inconsistent with the experience of other funds invested in this area.

SECTION 5
Schroder Investment Management
Property Portfolio Performance

Performance

	One Year	From Aug 2007 (% p.a.)
Portfolio	-2.4	-3.9
Benchmark	11.6	-12.0
Relative Return	-12.6	9.2

Key Points

Latest Year

> In the latest year the portfolio return of -2.4% underperformed the benchmark by 12.6%.

> The UK property assets held by the portfolio continued to underperform the IPD index, However the key reason the portfolio underperformed was the poor return from its overseas investments which was depressed by the weakness of the Euro.

> The portfolio also lost performance from holding some of the assets as cash.

Longer Term

> Since August 2007 the portfolio has returned -3.9% p.a., well ahead of benchmark. This was primarily due to the strong performance of the overseas investments in 2008/09.

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> Shetland Islands Council Capital and Miscellaneous Funds

SECTION 6
Baillie Gifford
Capital Fund Performance

Portfolio Benchmark and Target

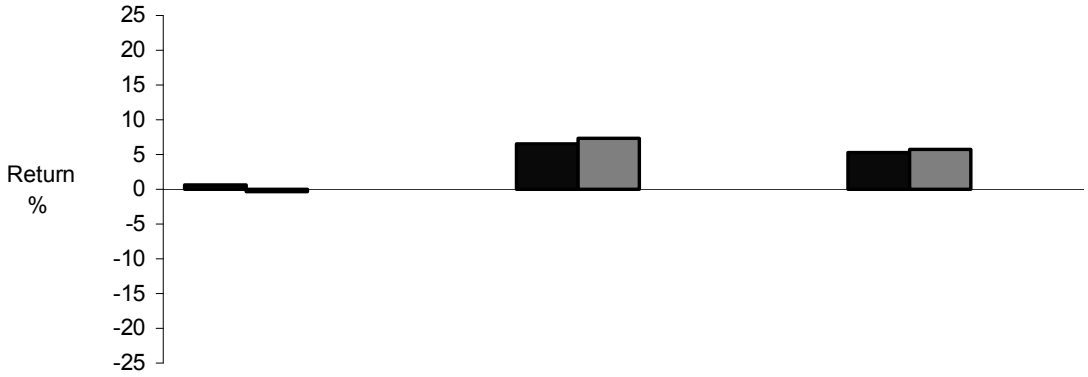
Benchmark

> The performance of Baillie Gifford is measured against a customised Benchmark compromised 90% of the FT-A 5-15 year UK gilt index and 10% of the cash index (LIBID).

Target

> The target of the portfolio is to outperform the benchmark by 0.3% pa over five year periods.

Performance



	1 Year	3 Years % pa	5 Years % pa
Fund	0.6	6.5	5.3
Benchmark	-0.3	7.3	5.7
Relative Return	0.9	-0.7	-0.4

Attribution Analysis

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
Fund Returns															
Fund	-1.8	4.0	3.8	0.7	-3.0	4.3	9.3	1.8	-1.5	2.0	-1.5	1.8	0.6	6.5	5.3
Benchmark	-2.0	4.3	4.4	2.4	-4.1	5.8	9.7	2.0	-1.7	1.3	-1.7	1.9	-0.3	7.3	5.7
Relative	0.3	-0.3	-0.5	-1.7	1.1	-1.4	-0.3	-0.2	0.1	0.7	0.2	-0.1	0.9	-0.7	-0.4
Asset Allocation															
Impact	0.1	-	-	-	0.1	-0.1	-0.2	-0.1	-	-0.1	-	0.1	-	-0.1	-0.1
Stock Selection															
Impact	0.2	-0.3	-0.5	-1.7	1.1	-1.3	-0.1	-0.1	0.1	0.8	0.2	-0.2	0.9	-0.6	-0.3

Asset Allocation

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
UK BONDS															
Fund	87.5	90.1	89.0	89.2	87.7	87.3	88.3	89.3	88.1	89.6	89.0	90.0			
Benchmark	90.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0			
Impact	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
CASH															
Fund	12.5	9.9	11.0	10.8	12.3	12.7	11.7	10.7	11.9	10.4	11.0	10.0			
Benchmark	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0			
Impact	-	-	-	-	-	-0.1	-0.2	-	-	-	-	-	-	-0.1	-0.1

Selection

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
UK BONDS															
Fund	-2.2	4.3	4.2	0.6	-3.6	4.7	10.5	2.0	-1.7	2.3	-1.7	1.8	0.5	6.9	5.5
Benchmark	-2.4	4.6	4.7	2.6	-4.7	6.3	10.6	2.2	-1.9	1.4	-1.9	2.1	-0.4	7.7	5.9
Impact	0.2	-0.3	-0.5	-1.7	1.0	-1.3	-0.1	-0.1	0.1	0.8	0.2	-0.2	0.8	-0.6	-0.4
CASH															
Fund	1.4	1.5	1.0	1.4	1.4	1.4	1.1	0.3	0.2	0.2	0.1	0.6	1.1	3.6	4.2
Benchmark	1.4	1.5	1.5	1.3	1.3	1.3	0.8	0.2	0.1	0.1	0.1	0.1	0.4	3.2	3.8
Impact	-	-	-	-	-	-	-	-	-	-	-	0.1	0.1	-	-

Key Points

Latest Year

> In the latest year the fund return of 0.6% was 0.9% above the benchmark of -0.3%.
> This was due relatively good bond stock selection in the last nine months of 2009.

Longer Term

> Over the last three years the portfolio returned 6.5% pa, underperforming by 0.7% pa.

> Over the last five years the portfolio has underperformed by 0.4% pa. This means that performance is 0.7% pa below the added value target that was set.
>
> Over both these periods the reason for underperformance was relatively poor bond selection.

SECTION 7
Baillie Gifford
Miscellaneous Fund Performance

Benchmark and Target

Benchmark

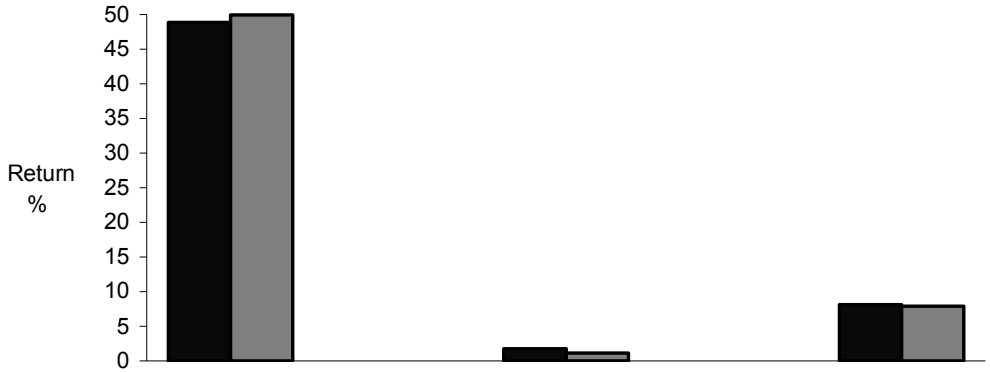
> Baillie Gifford's performance is measured against a customised benchmark:

	Weighting (%)	Benchmark
UK Equities	75.0	FTSE All Share
Overseas Equities	23.0	
North America	*6.325*	*FTSE North America*
Europe	*6.325*	*FTSE Europe ex UK*
Total Far East	*9.2*	*FTSE AW Dev Asia Pacific inc Japan*
Emerging Markets	*1.15*	*IFC Investable*
Cash	2.0	LIBID 7 Day

Target

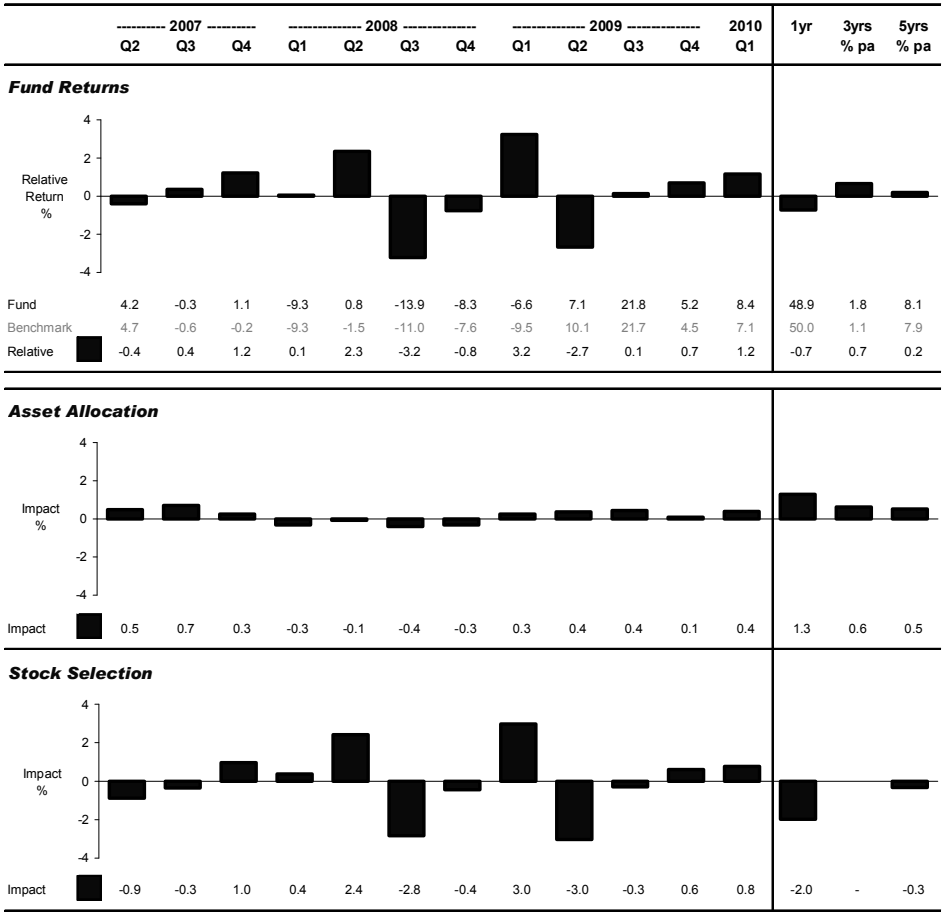
> The target of the Fund is to outperform the benchmark by 1.5% pa over five year periods.

Performance



	1 Year	3 Years % pa	5 Years % pa
Fund	48.9	1.8	8.1
Benchmark	50.0	1.1	7.9
Relative Return	-0.7	0.7	0.2

Attribution Analysis



	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
Fund Returns															
Fund	4.2	-0.3	1.1	-9.3	0.8	-13.9	-8.3	-6.6	7.1	21.8	5.2	8.4	48.9	1.8	8.1
Benchmark	4.7	-0.6	-0.2	-9.3	-1.5	-11.0	-7.6	-9.5	10.1	21.7	4.5	7.1	50.0	1.1	7.9
Relative	-0.4	0.4	1.2	0.1	2.3	-3.2	-0.8	3.2	-2.7	0.1	0.7	1.2	-0.7	0.7	0.2
Asset Allocation															
Impact	0.5	0.7	0.3	-0.3	-0.1	-0.4	-0.3	0.3	0.4	0.4	0.1	0.4	1.3	0.6	0.5
Stock Selection															
Impact	-0.9	-0.3	1.0	0.4	2.4	-2.8	-0.4	3.0	-3.0	-0.3	0.6	0.8	-2.0	-	-0.3

Asset Allocation

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
U.K. EQUITIES															
Fund	71.7	69.8	70.3	70.2	70.2	69.6	68.7	68.6	67.7	67.4	65.1	64.6			
Benchmark	75.0	75.0	75.0	75.0	75.0	75.0	75.0	75.0	75.0	75.0	75.0	75.0			
Impact	-	-	-	-	-	0.1	0.1	-	-	-	-0.1	0.1	-0.1	-	-
NORTH AMERICA															
Fund	7.7	7.9	7.9	7.9	8.4	9.3	9.2	9.3	8.5	8.0	8.7	9.0			
Benchmark	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3			
Impact	-	-	-	-	-	0.3	0.1	-	-0.2	-	-	0.1	-0.2	0.1	-
CONTINENTAL EUROPE															
Fund	6.5	6.5	6.5	6.9	6.3	6.7	6.9	6.6	6.8	7.2	7.6	7.5			
Benchmark	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3			
Impact	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL FAR EAST															
Fund	7.4	8.0	7.9	7.8	7.9	7.9	8.9	8.8	9.1	9.1	9.5	9.9			
Benchmark	9.2	9.2	9.2	9.2	9.2	9.2	9.2	9.2	9.2	9.2	9.2	9.2			
Impact	-	-	0.1	-	-	-	-0.2	-	-	-	-	-	-	-0.1	-
EMERGING MARKETS															
Fund	6.8	7.8	7.4	7.3	7.2	6.6	6.2	6.8	7.9	8.3	9.1	9.0			
Benchmark	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2			
Impact	0.4	0.7	0.4	-0.1	-	-0.5	-0.2	0.6	0.4	0.2	0.2	0.1	1.0	0.8	0.5
CASH/ALTERNATIVES															
Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0			
Benchmark	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0			
Impact	0.1	-	-0.1	-0.2	-	-0.2	-0.2	-0.3	0.2	0.3	-	0.1	0.6	-0.1	-

Stock Selection

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
U.K. EQUITIES															
Fund	3.5	-2.7	0.4	-9.4	0.9	-14.9	-9.6	-6.8	5.6	21.3	5.7	7.4	45.3	-1.3	6.0
Benchmark	4.5	-1.8	-0.3	-9.9	-1.4	-12.2	-10.2	-9.1	10.9	22.4	5.5	6.4	52.3	-0.2	7.2
Impact	-0.7	-0.7	0.5	0.4	1.6	-2.1	0.4	1.9	-3.3	-0.6	0.1	0.6	-3.2	-0.6	-0.7
NORTH AMERICA															
Fund	4.1	2.2	3.3	-9.2	7.5	-5.0	-8.2	-5.3	-0.1	15.7	6.6	12.8	39.1	7.2	7.9
Benchmark	4.3	1.1	-0.6	-9.1	-1.6	1.4	-4.5	-9.8	1.8	19.3	4.8	12.5	43.2	5.4	7.6
Impact	-	0.1	0.3	-	0.7	-0.6	-0.4	0.4	-0.2	-0.3	0.1	-	-0.2	0.1	-
CONTINENTAL EUROPE															
Fund	6.0	-0.5	0.2	-4.3	-7.1	-9.4	-4.7	-11.4	10.5	28.3	3.7	7.2	57.5	4.2	11.7
Benchmark	7.0	0.8	3.0	-7.4	-5.2	-11.2	-2.5	-16.0	9.9	29.5	0.6	4.0	48.8	1.8	10.0
Impact	-0.1	-0.1	-0.2	0.2	-0.1	0.1	-0.2	0.3	-	-0.1	0.2	0.2	0.4	0.2	0.1
TOTAL FAR EAST															
Fund	2.3	7.9	0.0	-11.1	1.6	-12.9	4.2	-8.4	10.8	22.0	1.5	13.3	55.4	8.8	13.3
Benchmark	3.9	4.5	-1.6	-8.7	-0.3	-12.0	6.5	-11.5	10.4	16.6	-0.2	12.7	44.7	5.2	10.9
Impact	-0.1	0.2	0.1	-0.2	0.2	-0.1	-0.2	0.3	-	0.4	0.1	0.1	0.6	0.3	0.2
EMERGING MARKETS															
Fund	13.1	14.1	9.4	-11.1	-1.0	-20.9	-13.2	1.1	24.1	27.8	7.7	7.3	83.3	16.5	24.1
Benchmark	13.1	11.9	6.3	-11.1	-1.2	-18.4	-10.6	1.6	18.4	24.5	7.6	9.3	73.4	14.9	21.9
Impact	-	0.1	0.2	-	-	-0.2	-0.2	-	0.3	0.2	-	-0.2	0.4	0.1	0.1

Key Points

Latest Year

> In the latest year the portfolio return of 48.9% was 0.7% below the benchmark.

> This was due to asset allocation, particularly the high weighting to emerging markets and decision to hold no cash.

> UK stock selection was very poor, offsetting the good result from this area in the previous year.

Longer Term

> Over the last three years the portfolio returned 1.8% pa, outperforming the benchmark by 0.7% pa.

> Over the last five years the portfolio has outperformed by 0.2% pa with a return of 8.1% pa. Over this period performance was 1.3% pa below the added value target that was set.

SECTION 8
Insight
Miscellaneous Fund Performance

Benchmark and Target

Benchmark

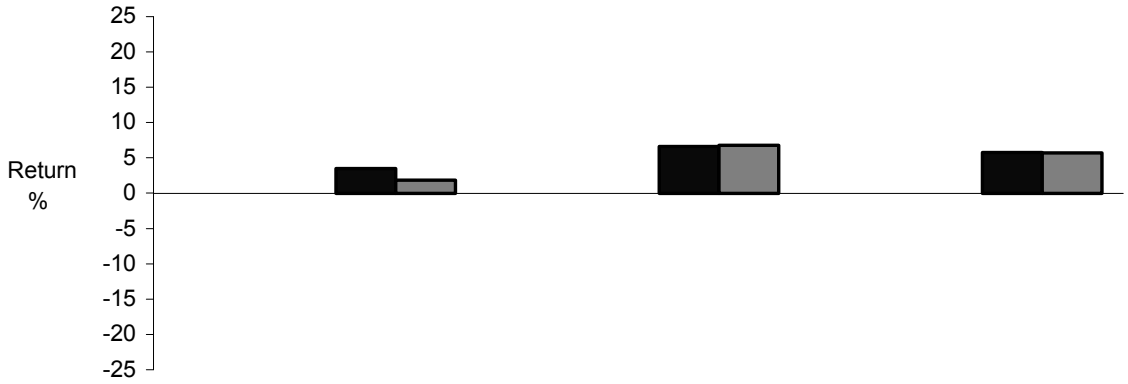
> Insight's performance is measured against a customised benchmark:

	Weighting (%)	Benchmark
UK Bonds	60.0	FT-A 5-15 Year Gilts
UK Index Linked	20.0	FT-A Index Linked All Stocks
Cash	20.0	LIBID 7 Day

Target

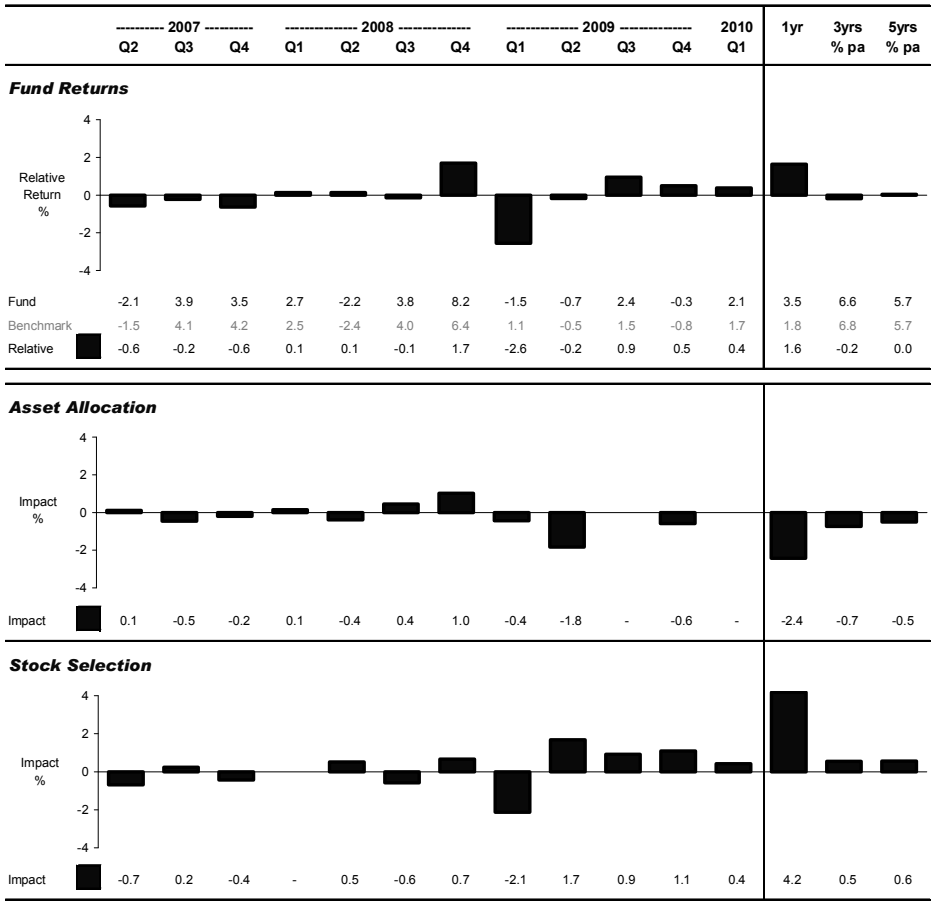
> The target of the portfolio is to outperform the benchmark by 0.5% pa over five year periods.

Performance



	1 Year	3 Years % pa	5 Years % pa
Fund	3.5	6.6	5.7
Benchmark	1.8	6.8	5.7
Relative Return	1.6	-0.2	0.0

Attribution Analysis



	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
Fund Returns															
Fund	-2.1	3.9	3.5	2.7	-2.2	3.8	8.2	-1.5	-0.7	2.4	-0.3	2.1	3.5	6.6	5.7
Benchmark	-1.5	4.1	4.2	2.5	-2.4	4.0	6.4	1.1	-0.5	1.5	-0.8	1.7	1.8	6.8	5.7
Relative	-0.6	-0.2	-0.6	0.1	0.1	-0.1	1.7	-2.6	-0.2	0.9	0.5	0.4	1.6	-0.2	0.0
Asset Allocation															
Impact	0.1	-0.5	-0.2	0.1	-0.4	0.4	1.0	-0.4	-1.8	-	-0.6	-	-2.4	-0.7	-0.5
Stock Selection															
Impact	-0.7	0.2	-0.4	-	0.5	-0.6	0.7	-2.1	1.7	0.9	1.1	0.4	4.2	0.5	0.6

Asset Allocation

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
U.K. BONDS															
Fund	68.7	69.1	69.2	68.4	66.7	66.4	58.3	51.2	48.9	54.3	58.1	57.5			
Benchmark	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0			
Impact	-0.1	-	-	-	-0.2	0.1	0.2	-0.1	0.1	-	0.1	-	0.2	0.1	0.1
OVERSEAS BONDS															
Fund					0.6	0.2	0.3	8.9	12.0	4.3	0.0				
Benchmark															
Impact					-0.1	-	-	-0.4	-1.8	0.1	-0.8		-2.5	-1.0	-0.6
U.K. INDEX - LINKED															
Fund	11.0	11.0	11.2	11.4	11.1	10.9	20.3	17.5	18.1	18.3	18.6	20.0			
Benchmark	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0			
Impact	-	-0.1	-0.1	-0.1	-0.3	0.3	0.9	-0.1	-0.1	-	-	-	-0.1	0.2	0.1
CASH/ALTERNATIVES															
Fund	20.2	20.1	20.0	20.4	21.6	22.5	21.1	22.3	20.9	23.1	23.4	22.4			
Benchmark	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0			
Impact	-	-	-	-	-	-	-0.1	-0.1	-	-	-	-	-	-0.1	-0.1

Stock Selection

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	3yrs % pa	5yrs % pa
U.K. BONDS															
Fund	-3.3	5.0	5.0	3.6	-3.9	5.4	11.4	-1.5	-0.9	3.0	-0.1	2.6	4.6	8.7	6.9
Benchmark	-2.4	4.6	4.7	2.6	-4.7	6.3	10.6	2.2	-1.9	1.4	-1.9	2.1	-0.4	7.7	5.9
Impact	-0.6	0.2	0.2	0.7	0.6	-0.6	0.4	-2.0	0.5	0.9	0.9	0.3	2.7	0.5	0.5
OVERSEAS BONDS															
Fund					-4.8 #	-0.5	25.1	-17.6	-22.5	6.5	-7.6 #				
Benchmark															
Impact															
U.K. INDEX - LINKED															
Fund	-1.6	5.1	5.2	4.8	1.8	-0.2	0.1	-0.9	3.6	3.6	1.6	2.7	12.0	8.8	7.6
Benchmark	-1.5	5.1	5.4	3.7	1.1	-0.3	-0.7	-1.3	2.9	3.1	1.6	2.2	10.3	7.1	6.6
Impact	-	-	-	0.1	0.1	-	0.2	0.1	0.1	0.1	-	0.1	0.3	0.2	0.2
CASH/ALTERNATIVES															
Fund	1.2	1.5	-1.7	-2.7	0.7	1.2	1.0	-0.7	4.8	-0.1	0.8	0.1	5.7	2.0	3.2
Benchmark	1.4	1.5	1.5	1.3	1.3	1.3	0.8	0.2	0.1	0.1	0.1	0.1	0.4	3.2	3.8
Impact	-	-	-0.6	-0.8	-0.1	-	0.1	-0.2	1.1	-	0.2	-	1.2	-0.2	-0.1

Key Points

Latest Year

> In the latest year the portfolio return of 3.5% was 1.6% above the benchmark.

> The key reason for the outperformance was the UK Bond selection. In a reversal of the previous year performance the UK Government bonds outperformed the benchmark index and the portfolio gained further benefit from holding corporate bonds throughout the year.

> Asset allocation had a negative effect. This was the result of the decision to hold overseas bonds where the portfolio performed very poorly during the year.

Longer Term

> Over the last three years the portfolio returned 6.6% pa, underperforming by 0.2% pa.

> Over the last five years the portfolio return of 5.7% pa was in line with benchmark but 0.5% pa below the added value performance target.

SECTION 9
GMO
Miscellaneous Fund Performance

Benchmark and Target

Benchmark

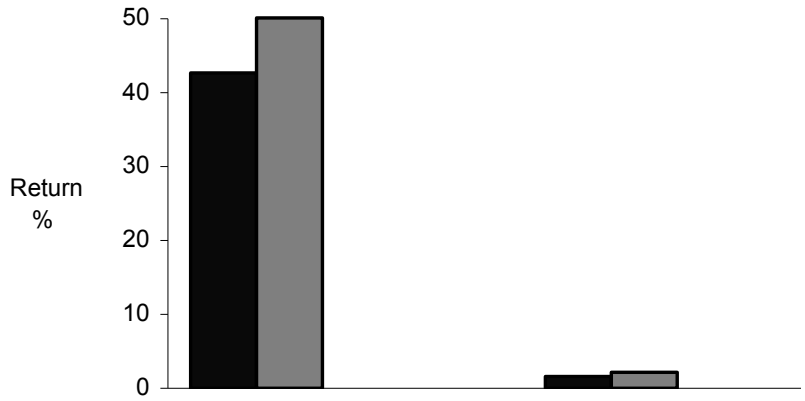
> The GMO performance is measured against a customised Benchmark:

	Weighting (%)	Benchmark
UK Equities	60.0	FTSE All Share
Overseas Equities	40.0	FTSE World ex UK

Target

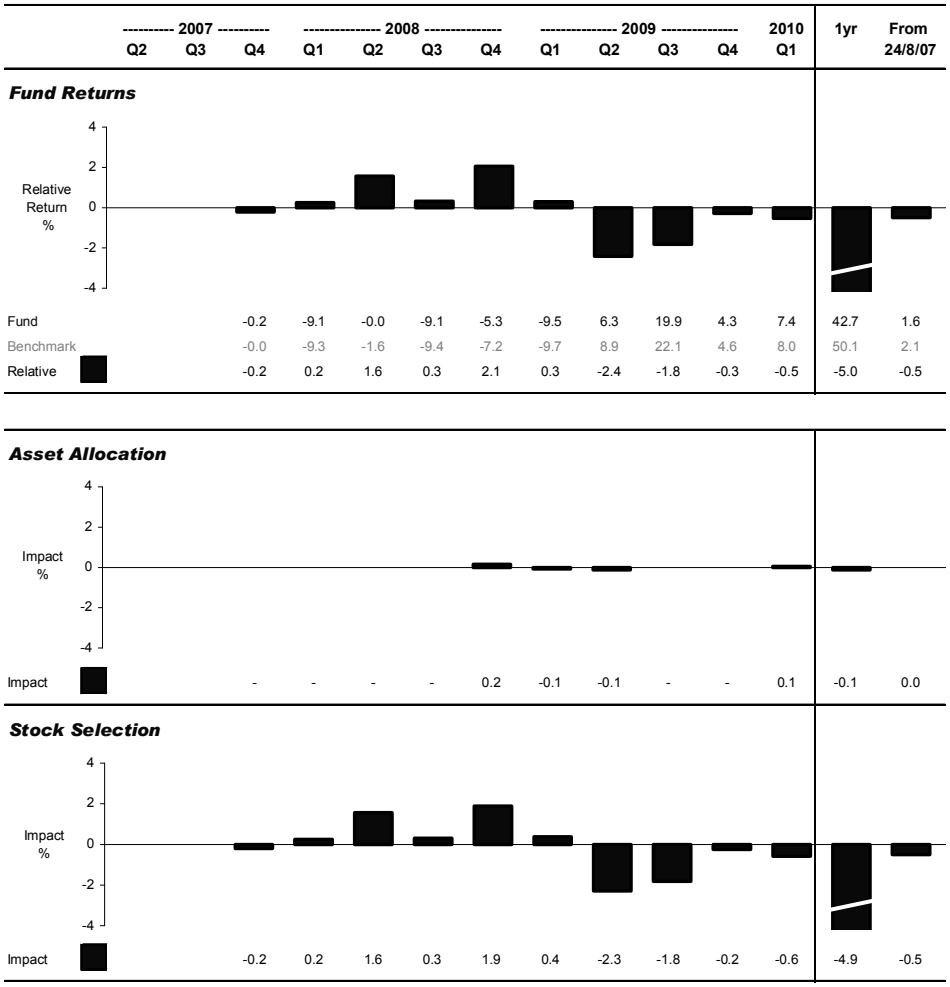
> The target of the portfolio is to outperform the benchmark by 1.0% pa over five year periods.

Performance



	1 Year	From 24/8/07 % pa
Fund	42.7	1.6
Benchmark	50.1	2.1
Relative Return	-5.0	-0.5

Attribution Analysis



	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	From 24/8/07
Fund Returns														
Fund			-0.2	-9.1	-0.0	-9.1	-5.3	-9.5	6.3	19.9	4.3	7.4	42.7	1.6
Benchmark			-0.0	-9.3	-1.6	-9.4	-7.2	-9.7	8.9	22.1	4.6	8.0	50.1	2.1
Relative			-0.2	0.2	1.6	0.3	2.1	0.3	-2.4	-1.8	-0.3	-0.5	-5.0	-0.5
Asset Allocation														
Impact			-	-	-	-	0.2	-0.1	-0.1	-	-	0.1	-0.1	0.0
Stock Selection														
Impact			-0.2	0.2	1.6	0.3	1.9	0.4	-2.3	-1.8	-0.2	-0.6	-4.9	-0.5

Asset Allocation

	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	1yr	From 24/8/07
U.K. EQUITIES														
Fund		59.9	59.8	59.4	60.0	57.9	56.1	57.2	58.4	58.1	58.5	57.9		
Benchmark			60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0		
Impact			-	-	-	-	0.1	-	-0.1	-	-	-	-	-
OVERSEAS EQUITIES														
Fund		40.1	40.2	40.6	40.0	42.1	43.9	42.8	41.6	41.9	41.5	42.1		
Benchmark			40.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0		
Impact			-	-	-	-	0.1	-	-0.1	-	-	-	-0.1	-

Stock Selection

	2007			2008				2009				2010	1yr	From
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1		24/8/07
U.K. EQUITIES														
Fund			-0.1	-9.7	0.9	-12.3	-8.2	-7.6	8.5	19.3	5.0	6.3	44.5	
Benchmark			-0.3	-9.9	-1.4	-12.2	-10.2	-9.1	10.9	22.4	5.5	6.4	52.3	
Impact			0.2	0.1	1.4	-0.1	1.3	0.9	-1.2	-1.5	-0.3	-0.1	-3.0	0.2
OVERSEAS EQUITIES														
Fund			-0.5	-8.2	-1.4	-4.3	-1.3	-11.8	3.2	20.8	3.3	8.9	40.2	
Benchmark			0.4	-8.5	-1.8	-5.2	-2.7	-10.7	5.9	21.7	3.2	10.3	46.8	
Impact			-0.4	0.1	0.2	0.4	0.6	-0.6	-1.1	-0.3	-	-0.5	-1.9	-0.7

Key Points

Latest Year

> In the latest year the portfolio return of 42.7% was 5.0% below benchmark.

> The key reason for the poor relative return was disappointing selection across both UK and overseas equities.

> Asset allocation had a neutral impact over the period

Longer Term

> Over the period from inception the portfolio returned 1.6% pa, underperforming by 0.5% pa.

> The underperformance was due to the disappointing equity results since early 2009.

Appendix

Relative Performance

> Q. Why are the relative return numbers in the report not simply the arithmetic difference between the fund and the benchmark?

> A. Whilst the ‘arithmetic’ difference adequately describes the relationship between a fund and benchmark, it is unsuitable for the construction of time series, quantifying growth in value or for inter-fund comparison.

> Whilst intuitively unappealing, a ‘geometric’ calculation overcomes these factors because it recognises the compounding effect of returns.

> This is best illustrated working through an example

An Example

A fund returns 7% each quarter, and the corresponding benchmark 5%.
Clearly the fund is 2% different (better) than benchmark each quarter and intuitively, 8% over the year, as below;

	Q1	Q2	Q3	Q4	Year
Portfolio	7.0	7.0	7.0	7.0	28.0
Benchmark	5.0	5.0	5.0	5.0	20.0
Difference	2.0	2.0	2.0	2.0	8.0

Applying these to a portfolio valued at £100 gives us;

	Value	Q1	Q2	Q3	Q4
Portfolio	100.0	107.0	114.5	122.5	131.1
Benchmark	100.0	105.0	110.3	115.8	121.6
% Diff'					7.8%

The compounding effect means that the difference in value isn't 8%, but 7.8%.

Shetland
Islands Council

REPORT

To: **Special Shetland Islands Council** **25 May 2010**

From: **Head of Finance**

Fund Management Annual Review 2009/10
Report No: F-026-F

1. Introduction

1.1 The purpose of this report is to inform Members on the position and performance of the Council's external investments with fund managers.

1.2 The Council has three fund managers with total investments, under management at the end of March 2010, of £231 million.

Funds under Management as at 31 March 2010

Manager	Fund	% of Reserves
Baillie Gifford – Capital Fund	Bond	17%
Insight Investment Management	Bond	17%
Baillie Gifford	Equity	31%
GMO	Equity	35%

1.3 Baillie Gifford, Insight and GMO will all give presentations at this Council meeting concerning their investment performance over the year to end March 2010. Baillie Gifford's presentation will cover both of the funds they manage.

1.4 Karen Thrumble will attend the meeting from WM Company, as they independently monitor the fund manager's performance. She will analyse each fund manager's performance relative to the markets they invest in before that Fund Manager presents to the Council.

1.5 Along with this report are attached the presentational documents from Baillie Gifford, Insight and GMO plus a performance report from the WM Company on the relevant funds.

1.6 In this report I will review each fund manager in turn and compare their performance in 2009/10 against the market performance where they were asked to invest, and also against the additional out performance target we asked them to achieve.

1.7 Due to the nature of the investments these managers are investing into, we take a long-term investment view, generally a five-year period. I will therefore not only look at each manager's performance over 2009/10 I will also look at their performance over a five year period, or from the inception of the mandate if that is shorter.

2. Links to Corporate Priorities

2.1 This report links to the Council's corporate priorities, defined in its Corporate Plan, specifically in relation to assisting the Council in ensuring the financial resources are managed so that the Council can sustain and develop the economy.

3. Risk Assessment

3.1 There is no risk associated with this report, as no decisions are required to be made. All investments carry some degree of investment risk but this can be minimised through diversification of fund managers, assets, benchmarks, markets, size of holdings etc.

4. Background

4.1 The external investments of the Council funds (i.e. other than those invested in the local economy) are co-ordinated by the Council's Treasury function. The Pension Fund and Charitable Trust's reserves, although not covered by this report, are also co-ordinated by the Council's Treasury function. This approach delivers a unified approach; ensures that all the funds benefit from the knowledge and experience of Council Officers; and provides useful comparisons.

4.2 The Council has always invested as per the regulations allowed under the Trustee Investment Act 1961. In effect the Council could only invest in certain specific UK bonds, various cash products and equities that met stated restrictive criteria. The Local Government in Scotland Act 2003 vested in Scottish Ministers the power to make new investment regulations for local authority funds. The Scottish Government have now used the 2003 Act to pass new investment

regulations, which allow the Council to invest its funds as per an investment strategy, duly approved by the Council each year before the start of the coming financial year. As the Scottish Government only passed the new regulations in March 2010 the Council has until 30 June 2010 to approve an investment strategy for the remainder of 2010/2011. Members will receive a report outlining a proposed strategy at the Council meeting on 30 June 2010.

4.3 The Funds, their managers, type of mandate and market value are listed below:

Fund	Manager	Mandate	Market Value (£m)	
			2010	2009
Capital	Baillie Gifford	Bonds	38	66
Miscellaneous	Insight	Bonds	39	41
Miscellaneous	GMO	Equity	82	57
Miscellaneous	Baillie Gifford	Equity	72	52
			231	216

4.4 The Miscellaneous Funds mentioned above are made up of the Renewals and Repairs Funds; the Reserve Fund; the Marine Fund; and the Insurance Fund.

4.5 During 2009/10 the value of the Council funds increased by £15 million.

4.6 In the main, this report concentrates on fund manager performance relative to the markets but we also need to consider the effect of any cash withdrawals or injections to the funds and the performance of the markets themselves. These influences can easily alter the absolute fund value.

4.7 The following table shows the effect on the fund due to withdrawals/additions and the investment return.

	SIC Funds £ million
As at 31.03.09	216
(Withdrawals)/Additions	(35)
Investment Return	50
As at 31.03.10	231

The figures show how the investment return or £50 million has benefited the overall investments during the year. This is a 23% return on the opening investment value. It also shows the volatile nature of investing over the short term, while over the long term the

returns are netted off to give a more balanced long-term figure. This investment return is a direct consequence of the world's major economies coming out of the recent economic recession.

The withdrawals from the SIC Funds totalled £35 million during the year, these withdrawals are required to cover the Council's revenue deficit and Capital works programme.

4.8 The 2009/10 market performance by asset class is set out below:

		%
Equities:	UK	52.3
	North America	43.2
	Europe	48.8
	Japan	29.6
	Pacific (Ex Japan)	67.2
	Emerging	74.5
Bonds:	UK	0.8
	UK Corporate	31.1
	Index-Linked	10.3
Property		16.3
Cash		0.4

As can be seen from the asset returns in 2009/10 equities produced some stellar returns with almost all regions returning over 40%, with the UK returning 52.3% and Pacific (Ex Japan) 67.2%. The fund manager has negligible influence over the market's return but they may be required by the mandate agreement to invest into these markets. The main constituent of a fund's performance is the market return, where the fund is invested. A fund manager is only asked to out perform the market return, i.e. a European equity scenario in 2009/10 where a fund manager is asked to out perform the market by 1% would equate to a 49.8% return.

4.9 This report reviews performance in 2009/10; a quick update for the start of this financial year 2010/11 shows a rather more unsettled global economic situation with concerns over economies such as Greece, Portugal and Spain dominating market sentiment.

5. Fund Manager Review

5.1 The rest of this report takes each mandate in turn and discusses manager performance.

5.2 A Fund Manager's performance is measured against a specific fund benchmark, which is made up of market indices of the countries where they invest.

5.3 A Fund Manager's target is a level of out performance above the benchmark that is seen as achievable with a low level of measured risk on a given mandate. The Manager will actively seek to produce investment returns in order to achieve the stated target. Performance at or above target is desirable but any returns above the benchmark will add value to the fund above the market return.

5.4 SIC Capital Fund – Baillie Gifford

5.4.1 Baillie Gifford has managed the Capital Fund since 1986. The Capital Fund in 2009/10 was restricted to investments allowed under the Trustee Investment Act 1961. In effect it could only be invested in certain bonds and cash.

5.4.2 Baillie Gifford's benchmark for this fund is based on 90% bonds and 10% cash. Their performance target for this fund is to beat this specific benchmark by 0.5% per annum.

5.4.3 The following table sets out in summary the performance of Baillie Gifford and Co versus the benchmark and the performance target in 2009/10, and also on a cumulative basis over a five-year investment period.

Fund Performance versus Benchmark and Target

	Fund Return (%)	Performance v Benchmark (%)	Performance v Target (%)
2009/10	0.6	0.9	0.4
Five years 05/06 to 09/10	29.5	-2.1	-3.5

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

The performance v target figure gives the percentage that the fund has out or under performed their set target.

5.4.4 The Capital Fund returned 0.6% in 2009/10 and it out performed the benchmark return by 0.9% and the target by 0.4%. The 0.6% return is small but it is a positive return given that the market returned -0.3% over the year.

5.4.5 On a cumulative basis over the five-year rolling monitoring period Baillie Gifford, are 2.1% below the overall benchmark return. This position is mainly due to their poor performance in 2007 and 2008, which is in contrast to their previous steady out performance.

5.5 SIC Miscellaneous Fund – Insight

5.5.1 The Bank of Scotland in line with many of the UK's main banks sold off certain non-core assets to raise cash, rationalise the business etc. During 2009/10 the Bank of Scotland sold Insight Investment Management, their fund management business to Bank of New York Mellon (BONYM). BONYM have various investment businesses throughout the world but generally leave the companies alone to continue with their specialist services. Hymans Robertson were consulted and they were positive on this sale, as BONYM did not own a UK investment house with Insight's specialities, and they were aware of BONYM's history of buying good companies and leaving them alone. No issues or problems were incurred around the take-over with the mandate, or since the ownership change.

5.5.2 Insight's benchmark for this fund is based on 80% bonds and 20% cash. Their performance target for this fund is to beat this specific benchmark by 0.5% per annum.

5.5.3 The following table sets out in summary the performance of Insight versus the benchmark and the performance target in 2009/10, and also on a cumulative basis over a five-year investment period.

Fund Performance versus Benchmark and Target

	Fund Return (%)	Performance v Benchmark (%)	Performance v Target (%)
2009/10	3.5	1.6	1.1
Five years 05/06 to 09/10	32.0	0.2	-2.3

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

The performance v target figure gives the percentage that the fund has out or under performed their set target.

5.5.4 The Miscellaneous Fund with Insight returned 3.5% in 2009/10, which was above the benchmark return by 1.6% and the target by 1.1%. This is a good strong performance by Insight above the market return.

5.5.5 On a cumulative basis over the five-year rolling monitoring period Insight is 0.2% above the overall benchmark return, though still below the target. The fund has over the five-year period increased in value by 32%, which is a good long-term bond return.

5.6 SIC Miscellaneous Fund – GMO

5.6.1 GMO were awarded this mandate in February 2007 and they started to manage this mandate in August 2007.

5.6.2 This fund is invested in equities and is split 60% UK equities and 40% overseas equities. The performance target for this fund is to beat this specific benchmark by 1.0% per annum.

5.6.3 The following table sets out in summary the performance of GMO versus the benchmark and the performance target in 2009/10, and also on a cumulative basis since inception.

Fund Performance versus Benchmark and Target

	Fund Return (%)	Performance v Benchmark (%)	Performance v Target (%)
2009/10	42.7	-5.0	-6.0
Two and a half years, Oct 07 to March 10	0.9	-0.9	-3.3

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

The performance v target figure gives the percentage that the fund has out or under performed their set target.

5.6.4 The Miscellaneous Fund with GMO has under performed the benchmark return by 5.0% and the target by 6.0% during a year where equity markets rose. The fund in real terms has increased in value by 42.7%, which is a remarkable amount but is below the market return.

5.6.5 On a cumulative basis over the two and a half year rolling monitoring period GMO is now 0.9% below the overall benchmark return and 3.3% below the target return. This under performance is mainly due to 2009/10 when equity markets rose and GMO lagged the market return. GMO have now given away all the out performance they achieved in the first year and a half of this mandate.

5.7 SIC Miscellaneous Fund – Baillie Gifford

5.7.1 Baillie Gifford has managed this fund since 2001. The benchmark for this fund is based on 75% UK equities, 23% overseas equities and 2% cash. Their performance target for this fund is to beat this specific benchmark by 1.5% per annum.

5.7.2 The following table sets out in summary the performance of Baillie Gifford and Co versus the benchmark and the performance target in 2009/10, and also on a cumulative basis over a five-year investment period.

Fund Performance versus Benchmark and Target

	Fund Return (%)	Performance v Benchmark (%)	Performance v Target (%)
2009/10	48.9	-0.7	-2.2
Five years 05/06 to 09/10	47.6	0.8	-6.4

The performance v benchmark figure gives the percentage that the fund has out or under performed the benchmark return (market indices).

The performance v target figure gives the percentage that the fund has out or under performed their set target.

5.7.3 Baillie Gifford has under performed the benchmark return by 0.7% and the target return by 2.2% during a year where equity markets rose. The fund in real terms has increased by 48.9% in value, which is a large percentage amount and shows the size of gains equity markets made in 2009/10.

5.7.4 Baillie Gifford is just above the benchmark return over the cumulative five year rolling monitoring period by 0.8% although below the target by 6.4%. Over the nine-year period since inception Baillie Gifford are cumulatively 8.3% above the benchmark return.

6. Financial Implications

6.1 Performance by a Fund Manager will have long-term financial consequences for the Council.

6.2 There are no decisions from this report, so there are no immediate financial consequences.

7. Policy and Delegated Authority

7.1 Day to day responsibility for Fund Management is delegated to the Head of Finance of Executive Services Department and/or his nominees (SIC 25 July 1996 minute reference 97/96). The Council retains responsibility for appointing Fund Managers and for regularly reviewing and questioning a Fund Managers performance (min ref 97/96). This report provides that opportunity.

8. Conclusions

8.1 Baillie Gifford (Capital Fund) out performed both the benchmark and the target in 2009/10 and added real value to the fund when the market produced a negative return. Cumulatively over the five-year monitoring period they are still below the benchmark return.

8.2 Insight (Miscellaneous Fund) out performed both the benchmark and the target in 2009/10 and added 3.5% in real value to the fund. Cumulatively over the five-year monitoring period Insight is 0.2% above the benchmark return and the fund has increased in value by 32.0%.

8.3 GMO has under performed the benchmark and the target in 2009/10. This has not been a good year for GMO but the fund due to the strong equity markets has risen 42.7% in value. Cumulatively over the two and a half year monitoring period GMO, due to 2009/10, have given away the out performance they had achieved over the first one and a half years of this mandate.

8.4 Baillie Gifford (Miscellaneous Fund) under performed the benchmark return and the target in 2009/10, but the fund increased in value by 48.9% during the year. Cumulatively over the five-year monitoring period they are above the benchmark return although below the target. Over the long-term Baillie Gifford are adding real value to the fund above the market return.

8.5 Overall the Council's fund managers have had mixed fortunes in 2009/10. The equity managers have under performed the equity markets but the funds have increased dramatically in value, as the equity markets rebounded strongly in 2009/10. The bond managers have out performed their respective markets but due to the almost flat bond market returns, the funds have only slightly increased in value over the year.

8.6 The Council's fund managers have witnessed a very different investment climate in 2009/10 to the one in 2008/09, where an ever changing and astonishing global economic crisis unfolded, and stock markets fell accordingly. In 2009/10 the market sentiment changed completely due to unprecedented intervention by governments, and the belief the major world economies would survive the crisis. This relief boosted investor confidence and quickly created a large recovery in the markets, with some very high market returns, e.g. the UK equity market increased by 52.3% in 2009/10. Generally the Council funds faired well in 2009/10 and the overall value of investments increased by £15 million.

9. Recommendations

9.1 I recommend the Council note with satisfaction the performance of Baillie Gifford (Capital Fund) and Insight (Miscellaneous Fund) in 2009/10.

9.2 I recommend the Council note with dissatisfaction the performance of Baillie Gifford (Miscellaneous Fund) and GMO (Miscellaneous Fund) in 2009/10.

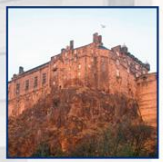
Date: 14 May 2010
Ref: CAB/DS Rep No: F-026-F

BAILLIE GIFFORD

Shetland Islands Council
Capital & Miscellaneous Funds

25th May 2010

Anthony Tait
Tom Wright



- Bond markets flat – fears of inflation and increased borrowing offset by economic uncertainty
- Stock markets stage recovery from their lows in March 2009
- Global economic recovery well underway
- Risks remain – government debt in the west, overheating in Emerging Markets
- Plentiful opportunities for stockpickers

Performance to 31st March 2010

	Fund	Benchmark	Difference
1 Year	**0.6**	**-0.3**	**+0.9**
5 Years (%p.a.)	**5.3**	**5.8**	**-0.5**
10 Years (% p.a.)	**5.4**	**5.7**	**-0.3**

Source: WM Performance Services/Baillie Gifford

- Bonds issued by the European Investment Bank performed better than UK Government bonds as investors became less risk averse

- Having relatively few 10 year bonds also helped as these bore the brunt of the sell off

Performance to 31st March 2010

	Fund	Benchmark	Difference
1 Year	**49.1**	**50.0**	**-0.9**
5 Years (%p.a.)	**8.2**	**7.9**	**+0.3**
Since Inception* (% p.a.)	**5.8**	**4.7**	**+1.1**

Source: WM Performance Services/Baillie Gifford

**22/03/01*

What Hurt?

- In UK equities having relatively little in the banking sector hurt during 2009/10 as prices recovered
- In oils, BG Group was weak and BP (not held) very strong during the year

What Helped?

- Good operating performance from most of the companies in the portfolio
- Exposure to Emerging Markets – BOC Hong Kong, BYD, Garanti Bankasi
- UK engineers also performed well – Meggitt, Weir Group

Bonds

- Government bonds offer very low yields and little protection against a return of inflation
- Significant levels of supply of fund government borrowing likely to depress future returns

Equities

- Opportunities in Emerging Markets and in those companies exposed to them
- Volatility likely to persist given uncertainties

Key Positions

- No significant change from last year
- Oils – prefer E&P and service companies to “majors”
  - BG Group, Cairn Energy, Petrobras
- Banks – still wary as huge uncertainties remain
  - Long term winners – Svenska Handelsbanken, Standard Chartered – should continue to prosper
  - Opportunities in Emerging Markets – Garanti Bankasi, Itau Unibanco
- Long term growth businesses trading on low valuations
  - Nestlé, L’Oréal, Walgreen

Miscellaneous Fund	**31 Mar 09**	**31 Mar 10**	**10 May 10**
	%	**%**	**%**
UK Equities	**68.3**	**64.8**	**64.5**
Overseas	**31.7**	**35.2**	**35.5**
Total	**100.0**	**100.0**	**100.0**
Total Value	**£51,613,110**	**£72,453,576***	**£70,423,465**

Capital Fund	**31 Mar 09**	**31 Mar 10**	**10 May 10**
	%	**%**	**%**
Bonds	**89.3**	**90.0**	**90.2**
Cash & Deposits	**10.7**	**10.0**	**9.8**
Total	**100.0**	**100.0**	**100.0**
Total Value	**£65,498,756**	**£38,315,898***	**£38,531,369**

**£17m returned from the Capital Fund and £5m from the Miscellaneous Fund during the year*

- Fund management partnership, based in Edinburgh
- Long term investment approach
  - Managers of Capital Fund since 1986
  - Miscellaneous Fund since 2001
- Independence → stability which benefits our clients
  - Looking for opportunities in current volatile markets

Shetland Islands Council

April LaRusse
Catherine Mulvihill

25 May 2010

A BNY MELLON COMPANY℠

Insight INVESTMENT

Presenting team

April LaRusse **Senior Product Specialist, Fixed Income**

Catherine Mulvihill **Institutional Client Director**

Agenda

- Insight Investment
- Shetland Islands mandates
  - Performance summary
- Investment review and outlook
- Appendix

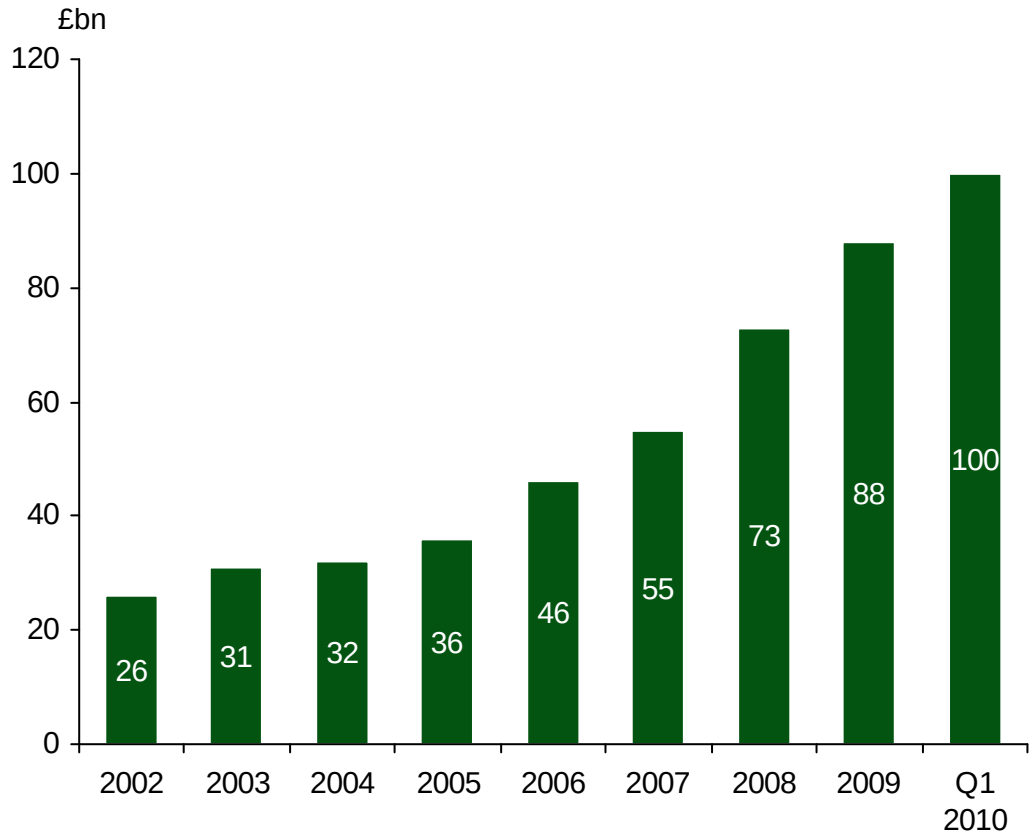
Insight INVESTMENT

Insight Investment

Insight Investment

- BNY Mellon Asset Management
  - Insight continues to operate on a stand-alone basis
  - backed by a triple-A rated (Moody's) institution committed to asset management
- Reputation for excellence in:
  - active fixed income
  - liability risk management
- £27.0bn of fixed income mandates[1]
- Largest manager of segregated mandates for UK pension funds[2]

Insight external AUM (GBP)[3]



[1] as at 31 December 2009
[2] FTfm, June 2009
[3] Source: Insight Investment as at 31 March 2010

Shetland Islands mandates

Mandate summary and investment restrictions

Shetland Islands Council Fund

Category	Index	Benchmark Weight (%)	Investment Ranges (%)
UK Government Bonds	FTSE Actuaries 5-15 years Gilt index	60	40 - 80
UK Index-Linked Bonds	FTSE Actuaries All Stocks Index-Linked Gilt index	20	10 - 30
Cash	Sterling 7 Day LIBID	20	10 - 30
Overseas bonds			0 - 20
UK Non-Government Bonds			0 - 30

Portfolio objective

- To outperform the benchmark by 0.5% per annum before fees, over rolling 5 year periods

Summary of performance

Shetland Islands Council Fund

Performance summary to 31 March 2010 (%)

	YTD 2010	1 year	3 years	5 years	Since Inception*
Portfolio	2.08	3.50	6.61	5.75	5.64
Benchmark	1.70	1.85	6.83	5.72	5.49
Relative Return	**0.38**	**1.65**	**-0.22**	**0.03**	**0.15**

Fund value

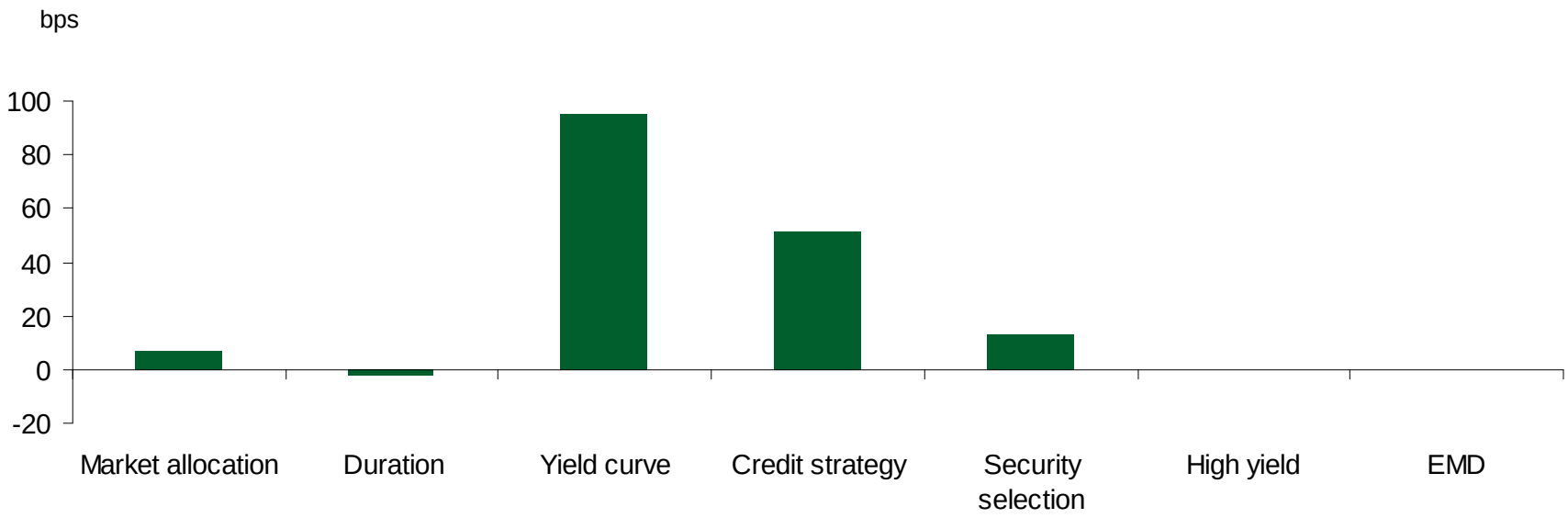
- Net asset value as at 31 March 2010: £38,970,308

All figures are gross of fees
Returns for periods greater than 1 year are annualised
Source: Insight Investment – IS405
*Inception date 31 March 2001

Shetland Islands Council Fund performance attribution

Contribution to relative returns

1 year to 31 March 2010



Mandate summary and investment restrictions

Shetland Islands Charitable Trust

Category	Index	Benchmark Weight (%)	Investment Ranges (%)
UK Government Bonds	FTSE A All-stocks Gilts Index	30	10 - 50
UK Non-Government Bonds	Merrill Lynch All-Stocks Sterling Non-Gilt Index	30	10 - 50
Overseas Bonds	JP Morgan World ex UK Govt Bond Index (£)	20	10 - 30
UK Index-Linked Bonds	FTSE A All-stocks Index-Inked Gilt Index	20	10 - 30
Cash			0 - 10

Portfolio objectives

- To outperform the benchmark by 0.5% per annum before fees, over rolling 5 year periods

Summary of performance

Shetland Islands Charitable Trust

Performance summary to 31 March 2010 (%)

	YTD 2010	1 year	3 years	5 years	Since Inception*
Portfolio	2.92	14.54	6.44	5.73	5.90
Benchmark	2.23	9.01	5.97	5.39	5.60
Relative Return	**0.69**	**5.53**	**0.47**	**0.34**	**0.30**

Fund value

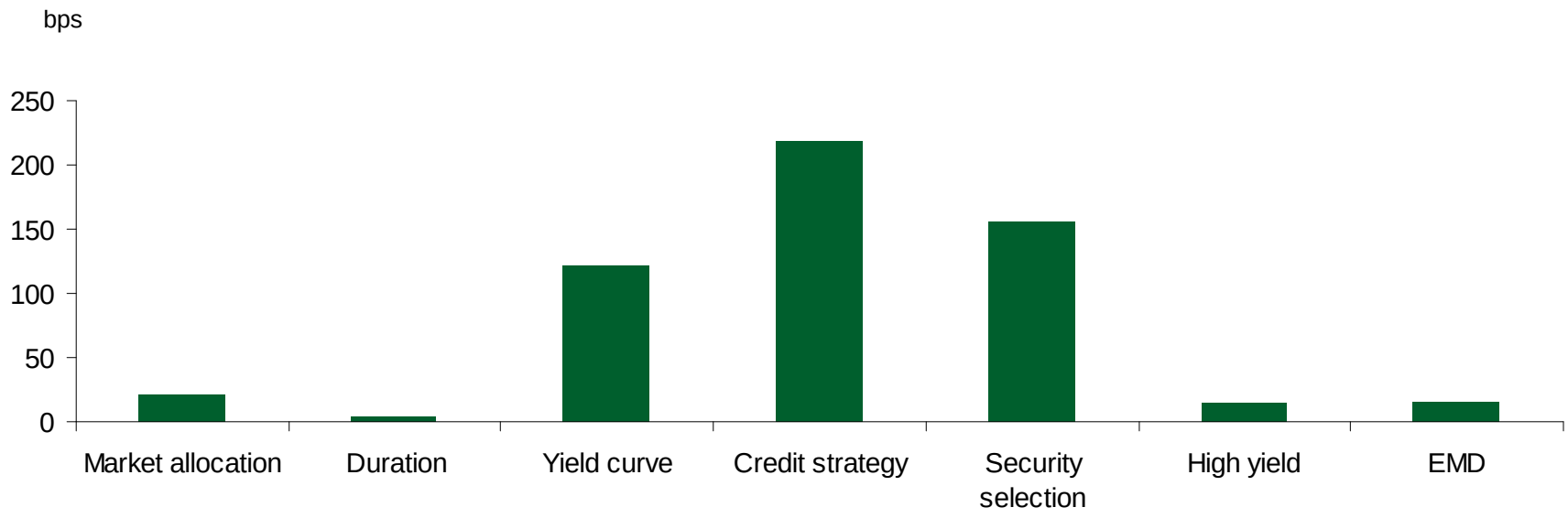
- Net asset value as at 31 March 2010: £46,859,491

All figures are gross of fees
Returns for periods greater than 1 year are annualised
Source: Insight Investment – IS401
*Inception date 7 October 2003

Shetland Islands Charitable Trust Fund performance attribution

Contribution to relative returns

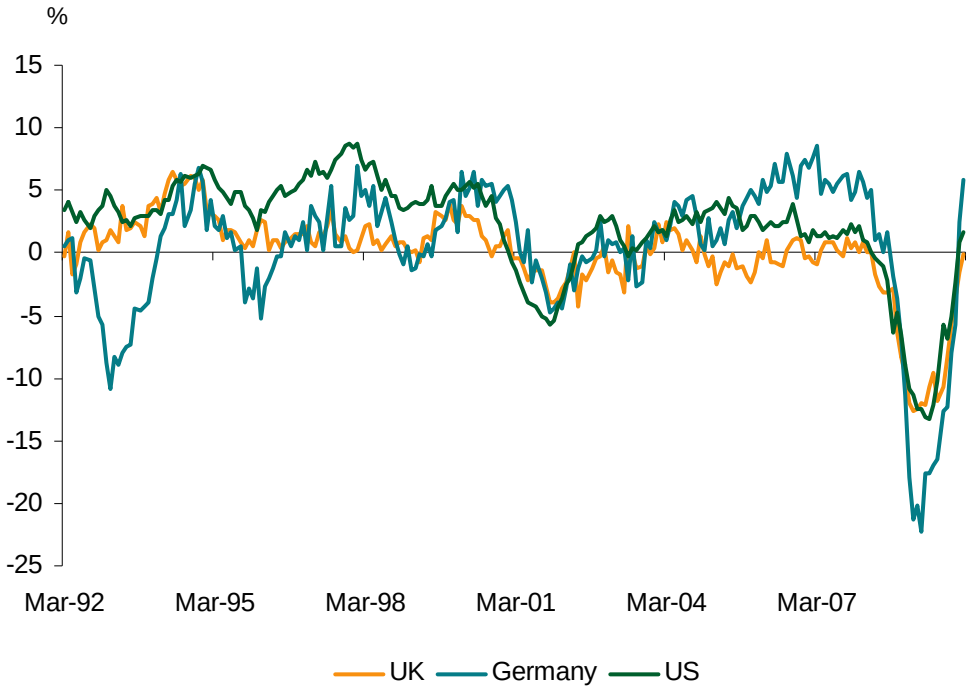
1 year to 31 March 2010



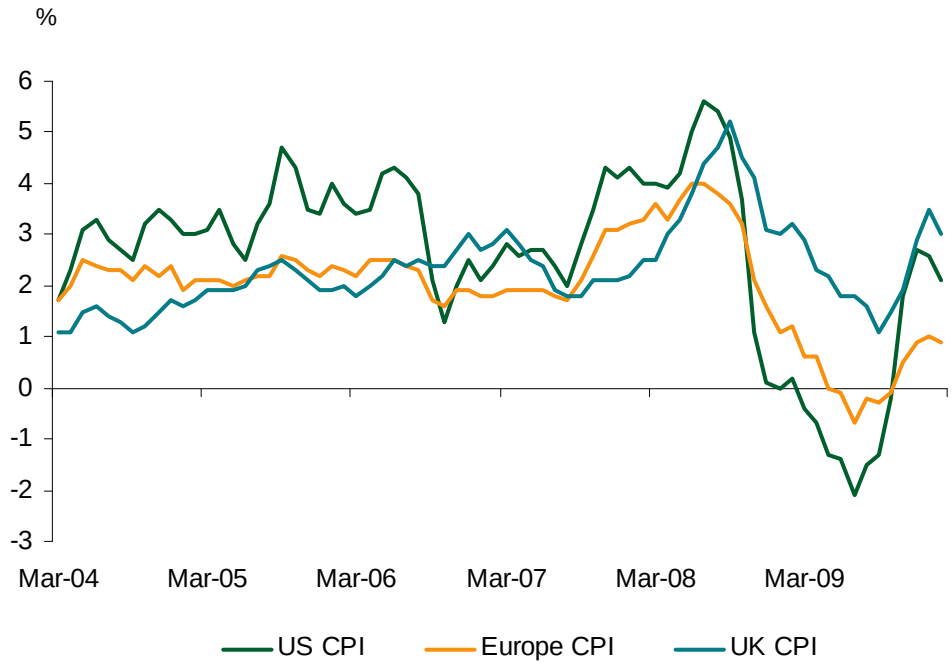
Investment review

Economic review
Global environment

Industrial production (yoy)



Inflation (yoy)



Source: Bloomberg, as at 31 March 2010

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UK government bonds

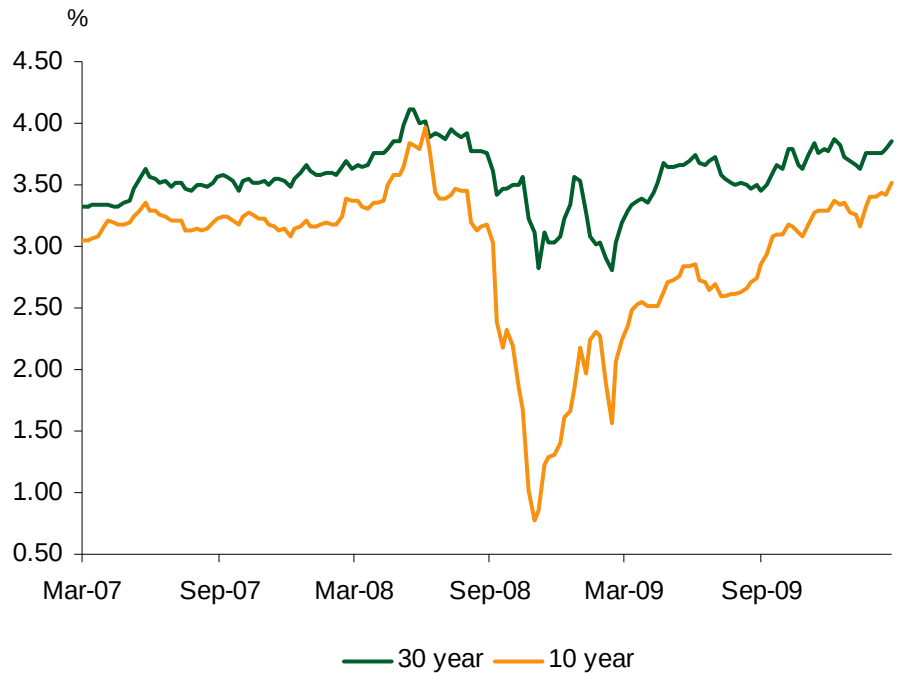
Yield history

Source: Bloomberg, as at 31 March 2010

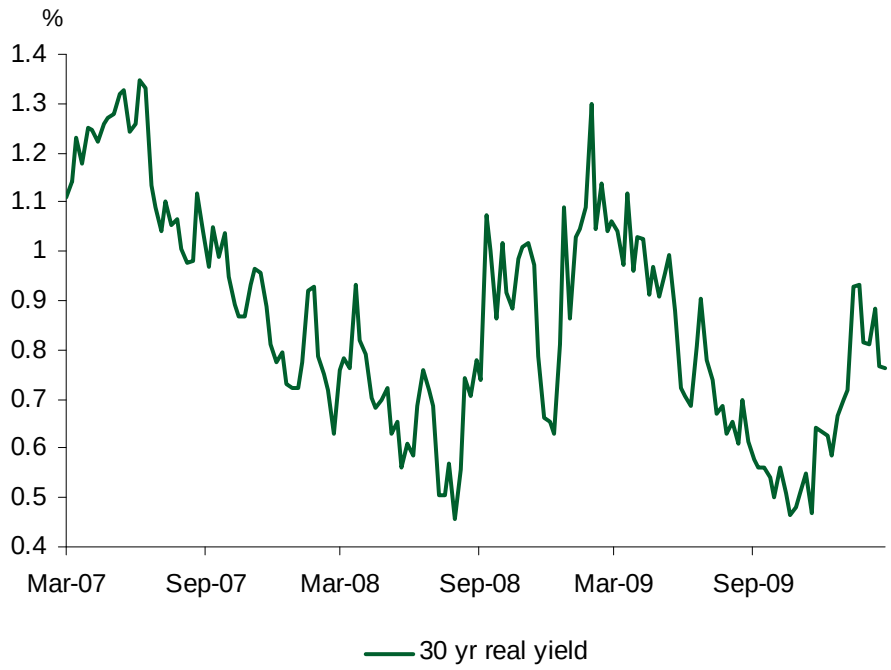
UK Index linked bonds

Index linked vs conventional gilts

10 year and 30 year breakeven inflation



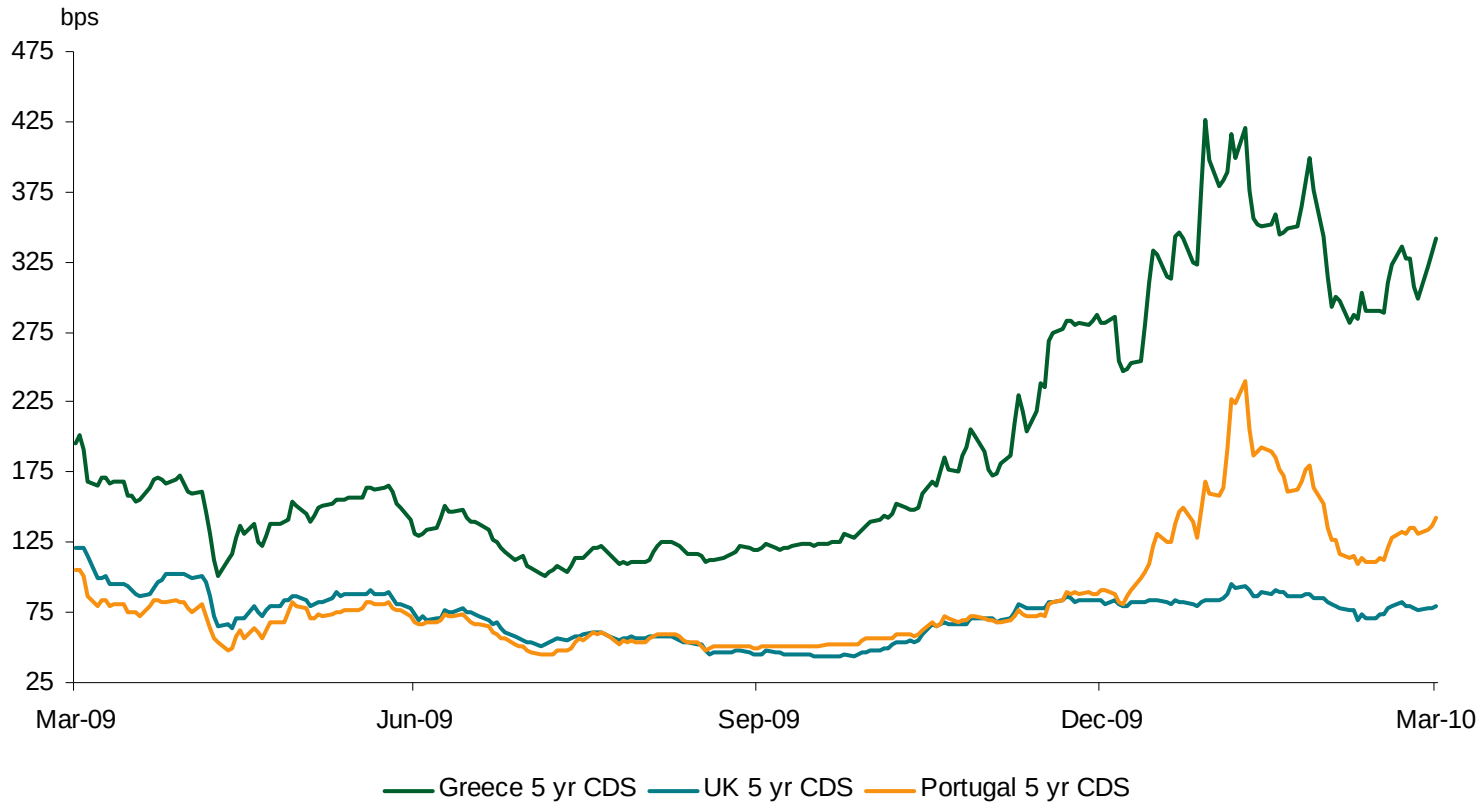
30 yr real yield



Source: Bloomberg, as at March 2010

Sovereign credit risk

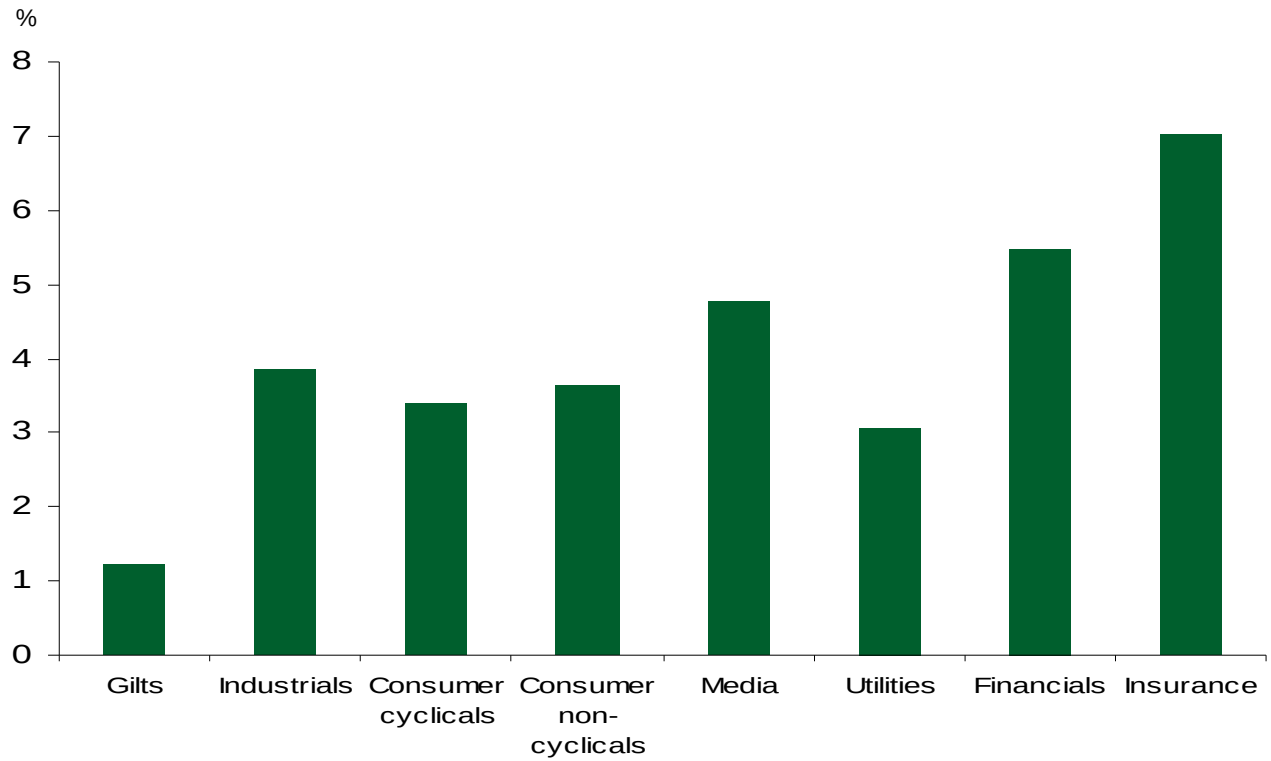
Cost of default risk insurance



Source: Bloomberg, as at 31 March 2010

UK corporate bonds
Sterling credit sectors

Sector total returns in Q1, 2010



Source: Merrill Lynch indices, Bloomberg, as at 31 March 2010

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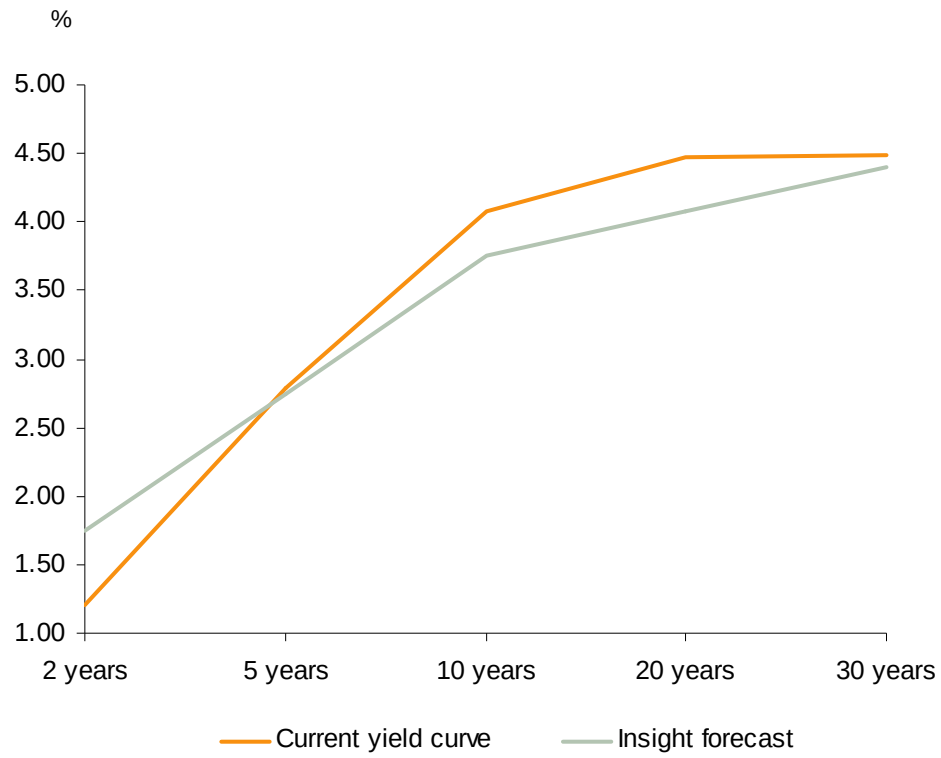
Outlook

UK government bonds

Where are they going?

	Current yield curve	Insight forecast
2 years	1.21	1.75
5 years	2.79	2.75
10 years	4.08	3.75
30 years	4.48	4.40

UK government yield curve vs Insight forecasts



Source: Insight, Bloomberg, as at 31 March 2010

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Economics

Market forecasts

12-month market forecast: bonds

Conventional	Official rates	2yr	5yr	10yr	30yr
UK	1.00	1.75	2.75	3.75	4.40
US	1.00	2.00	2.50	3.25	4.00
Europe	1.00	1.60	2.30	2.90	3.50
Japan	0.10	0.20	0.70	1.50	2.30

12-month market forecast: currency

Currency pair	Spot rate (31 March 2010)	Forecast
US$/Sterling	1.52	1.60
Sterling/Euro	0.89	0.86
US$/Euro	1.35	1.40
Yen/$	93.44	90.00
Can$/US$	1.02	1.10
US$/Aus$	0.92	0.90
S.African Rand/US$	7.34	8.00
Swedish Krone/Euro	9.74	10.00
Norwegian Krone/Euro	8.03	8.00

Source: Insight, as at 31 March 2010

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Thank you

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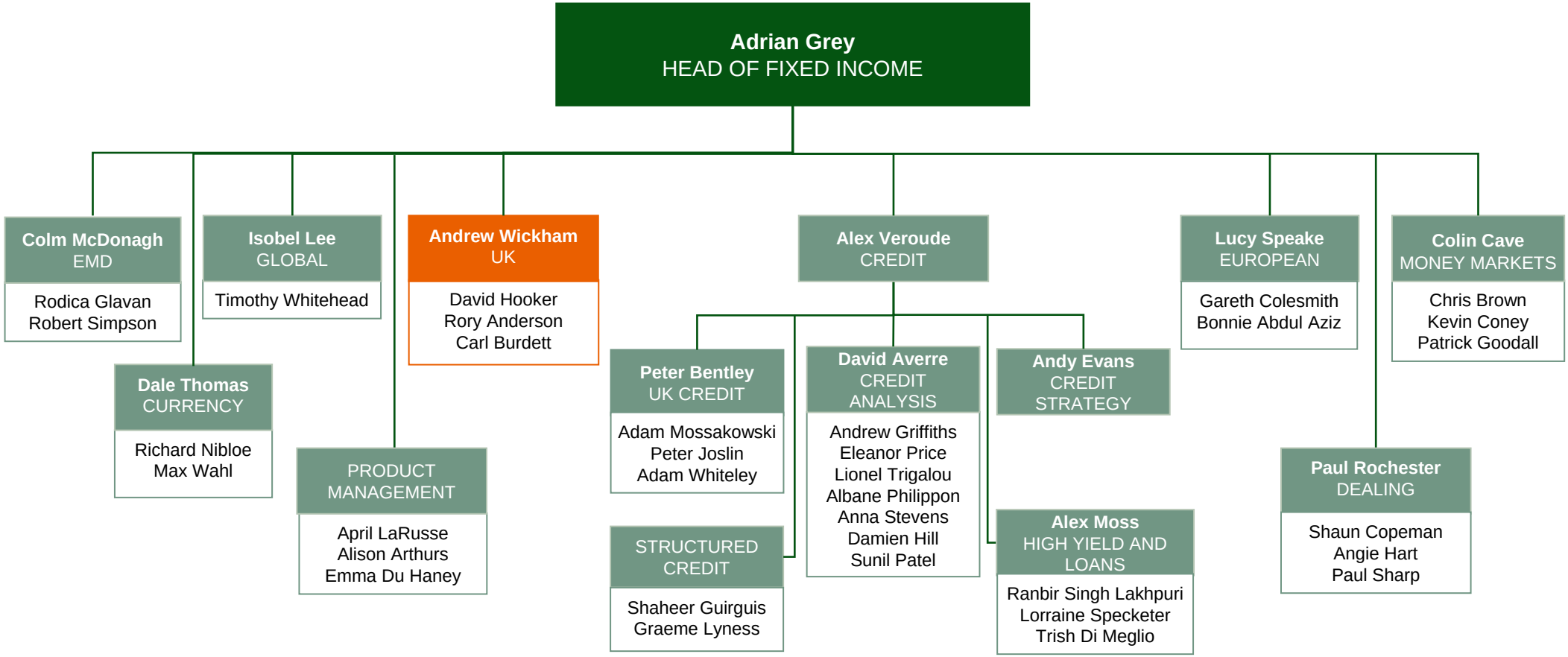
Appendix

Fixed income
Specialist teams



Source: Insight, as at April 2010

Portfolio analysis

Shetland Islands Council Funds

Portfolio summary	Fund (%)	Benchmark (%)
Financials	0.00	0.00
Gilts	52.75	60.31
Index-linked gilts	17.78	19.69
Supranationals	7.29	0.00
Cash	22.19	20.00
Total	**100.00**	**100.00**

Duration contribution	Fund (yrs)	Benchmark (yrs)
0-5 years	0.10	0.08
5-7 years	0.14	0.91
7-10 years	3.33	2.23
10 -15 years	1.62	1.83
15-25 years	0.69	0.87
25 years +	1.29	1.21
Total	**7.18**	**7.12**

	Fund	Benchmark
Yield (%)	2.33	2.25

Data as at 7 May 2010

Portfolio analysis

Shetland Islands Charitable Trust – UK portfolio

Portfolio summary	Fund (%)	Benchmark (%)
Financials	17.27	12.00
Gilts	26.91	37.88
Index-linked gilts	20.67	24.62
Industrials	9.18	7.05
Securitised	6.34	4.25
Supranationals	13.76	10.36
Utilities	2.79	3.84
Cash	3.09	0.00
Total	**100.00**	**100.00**

Duration contribution	Fund (yrs)	Benchmark (yrs)
0-5 years	0.61	0.65
5-7 years	0.07	0.55
7-10 years	1.74	1.10
10 -15 years	1.70	1.20
15-25 years	1.94	2.53
25 years +	3.18	3.27
Total	**9.23**	**9.31**

	Fund	Benchmark
Yield (%)	3.54	3.01

Data as at 7 May 2010

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Portfolio activity

Shetland Islands Charitable Trust – Overseas portfolio

Portfolio summary	Fund (%)	Benchmark (%)
Financials	6.01	0.00
Government conventionals	85.15	100.00
Industrials	2.44	0.00
Securitised	1.75	0.00
Supranationals	4.23	0.00
Utilities	0.54	0.00
Cash	-0.12	0.00
Total	**100.00**	**100.00**

	Fund	Benchmark
Yield (%)	2.78	1.89
Duration (yrs)	7.20	6.17

Data as at 7 May 2010

Country breakdown	Fund (%)	Benchmark (%)
Australia	0.37	0.86
Belgium	2.24	2.43
Canada	1.35	2.19
Denmark	0.00	0.85
Sweden	0.00	0.75
France	1.82	7.71
Germany	14.21	8.09
Ireland	1.15	0.00
Italy	10.25	7.93
Japan	21.91	31.73
Netherlands	4.36	2.10
Spain	0.00	3.56
Supranationals	1.44	0.00
EMD	3.51	0.00
UK	3.07	0.00
US	29.32	31.80
Cash	2.75	0.00

UK fixed income

Q1 2010 Performance attribution

	What we did…	What happened?	Impact
Market Allocation	• Reduced exposure to sterling supranationals • Tactical U/W in index linked vs conventional gilts • Maintained O/W in EMD	• Swaps and supranationals outperformed government bonds • Core EU bonds outperformed US and UK bonds • EMD outperformed • Breakeven inflation little changed despite volatility	• O/W supranationals and swaps relative to gilts was positive • EMD exposure was positive • Breakeven inflation position was positive
Duration and Curve	• Long duration position was maintained in Jan and Feb brought back to neutral before the Budget • Maintained overweight in 10yr and ultra long part of yield curve, but maintained underweight in 15-25 yr area • O/W intermediate dated index linked bonds	• UK 10 yr yields sold off sharply in Feb but ended the quarter unchanged • BoE buybacks ended. Focus moved to the scale of deficit to be funded in 2010/11 • UK yield curve steepened sharply with with short yields 15bps lower and 30 yr yields 10-15bps higher	• Duration positioning was positive for performance • Yield curve factors were negative in conventional funds and IL funds
Credit Strategy	• Modest O/W in credit risk • Overweight in physical IG credit • Reduced size of iTraxx credit hedge. • Remained overweight financials (banks and insurance), industrials and RMBS • Reduced senior bank paper into LT2 banks, property and insurance. Continued switching low yielding euro credit into sterling and US dollar denominated credit • Maintained exposure to short dated HY assets and increased loan exposure after the sell off	• Subordinated financials outperformed all other sectors • Real estate and basic industrials also performed well • More defensive sectors such as utilities and consumer non cyclicals lagged • ABS markets continued to rally. • High yield bonds continued to rally and new issuance was well received • Loans recovered after a sell off early in the quarter	• O/W credit risk was positive for performance. • Overweight in financials was a positive for performance • Positive impact from basic industrials, real estate, and capital goods sectors • Loan and HY positions positive • ABS also positive
Security Selection			
Currency Selection	• We continue to favour “growth” currencies (i.e. AUD, CAD, NOK etc) versus U/W in the Euro	• The Euro weakened vs most other currencies given the sovereign debt concerns	• U/W Euro vs AUD and CAD contributed to performance

UK fixed income

Q2 2010 Investment outlook

Insight INVESTMENT

	Investment themes	Portfolio strategy
Market Allocation	• Continued market concerns about sovereign credit risk makes supranational exposure attractive as risk diversification tool • Yields in EMD and Loans makes these markets attractive on a stock by stock basis • UK breakeven inflation rates may remain elevated	• O/W IG credit risk relative to government bonds • Maintaining sterling denominated supranational bonds relative to gilts • Look for opportunities to switch UK into EU or US bonds at better levels • Maintain selected EMD and loan exposure
Duration and Curve	• Sub-trend growth and impending fiscal tightening will ensure official rates stay low • However concerns about budget deficits and a " hung parliament" may cause volatility in gilt yields • The extreme steepness of the UK yield curve already compensates for most of the risk • We continue to see strategic value in 10 yr gilts at current yield levels. • Increased issuance in index linked will help rebalance the supply/demand mismatch in that market	• Looking to reset long duration positions given the amount of "bad news" already in the price of gilts • Adding to UK steepeners with an overweight focused in 10 yr bonds • Remain underweight 15-25 yr UK bonds • O/W medium dated index linked gilts
Credit Strategy	• IG credit is expected to generate higher total returns than government bonds but mostly due to higher overall yields so, most performance is expected to come from stock selection and relative value opportunities • We see better value in GBP and US dollar denominated paper than in European markets • Overweight in financials is now reduced and diversified away from banks into insurance • Reduced participation in new issues as they are no longer priced at a discount to secondary market levels and the quality of the companies is lower	• O/W IG credit risk but much reduced • Switching between Euro and GBP denominated bonds to enhance yield • Continuing to reduce exposure to senior bank bonds. • Selected profit taking on industrials which have seen substantial rallies • Reducing offsetting iTraxx index shorts where appropriate. • Adding risk in selected ABS bonds rotating out of senior into mezzanine • Increasing selected loans exposure where possible
Security Selection		
Currency Selection	• Cyclically sensitive currencies are preferred, funding them with short EUR, and increasingly short CHF and JPY	• Underweight Euro and Sterling in favour of AUD, NZD, CAD, NOK, BRL and PLN

Notes

Please note:

- All features in this pack are current at the time of publication but may be subject to change in the future.
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GMO

North America | Europe | Asia-Pacific

Shetland Islands Council

UK Equity Core
World Ex-UK Equities

25th May 2010

Portfolio Review

Presenting Team

Simon Harris, Partner, Head of Investment and Research, UK Core Portfolio Manager Simon joined GMO in 1989 and has been a partner since 1995. He heads the investment team and is responsible for the management of UK equity core portfolios. He is also the Chair of the Portfolio Management Committee in London. Simon holds a BSc in Mathematics from The City University, London and is a Fellow of the Securities Institute.

Nicholas Burgoyne, Director Client Relationship Management Nicholas joined GMO in 2004 as Head of Client Relationship Management in the UK. Nicholas has 30 years of experience in the financial sector in London, working as a portfolio manager and in client services. Nicholas has an MBA from the Open University.

Agenda

- Investment Process Reminder
- Performance Review
- Outlook & Portfolio Positioning
- Current Research Priority: Momentum

Shetland Islands Council

Performance in GBP, Net of Fees, Periods Ending 31st March 2010

Investment	Month	Quarter	YTD	Annualized 1 Year	3 Year	5 Year	Since Inception*	Market Value (M)	% of Account
UK Equity Core (08/24/2007)	6.79%	6.32 %	6.32%	44.46%	N/A%	N/A %	0.24 %	47.5	57.9%
FTSE All-Share Index	6.76	6.42	6.42	52.30	N/A	N/A	0.04		
Value Added	0.03	-0.10	-0.10	-7.84	N/A	N/A	0.20		
Domestic Equity (08/24/2007)	**6.79**	**6.32**	**6.32**	**44.46**	**N/A**	**N/A**	**0.24**	**47.5**	**57.9**
World ex-UK Equity (08/24/2007)	7.24	8.89	8.89	40.23	N/A	N/A	3.55	34.5	42.1
FTSE World ex-UK Index	6.92	10.27	10.27	46.76	N/A	N/A	5.18		
Value Added	0.32	-1.38	-1.38	-6.53	N/A	N/A	-1.63		
International Equity (08/24/2007)	**7.24**	**8.89**	**8.89**	**40.23**	**N/A**	**N/A**	**3.55**	**34.5**	**42.1**
Total Equity (08/24/2007)	**6.98**	**7.38**	**7.38**	**42.65**	**N/A**	**N/A**	**1.59**	**82.0**	**100.0**
Total Asset Allocation (08/24/2007)	**6.98**	**7.38**	**7.38**	**42.65**	**N/A**	**N/A**	**1.59**	**82.0**	**100.0**
Policy Benchmark **	6.82	7.96	7.96	50.14	N/A	N/A	2.15		
Value Added	0.16	-0.58	-0.58	-7.49	N/A	N/A	-0.56		

** Periods of less than a year are not annualized*

***** 60% FTSE All-Share Index/40% FTSE World ex-UK Index***

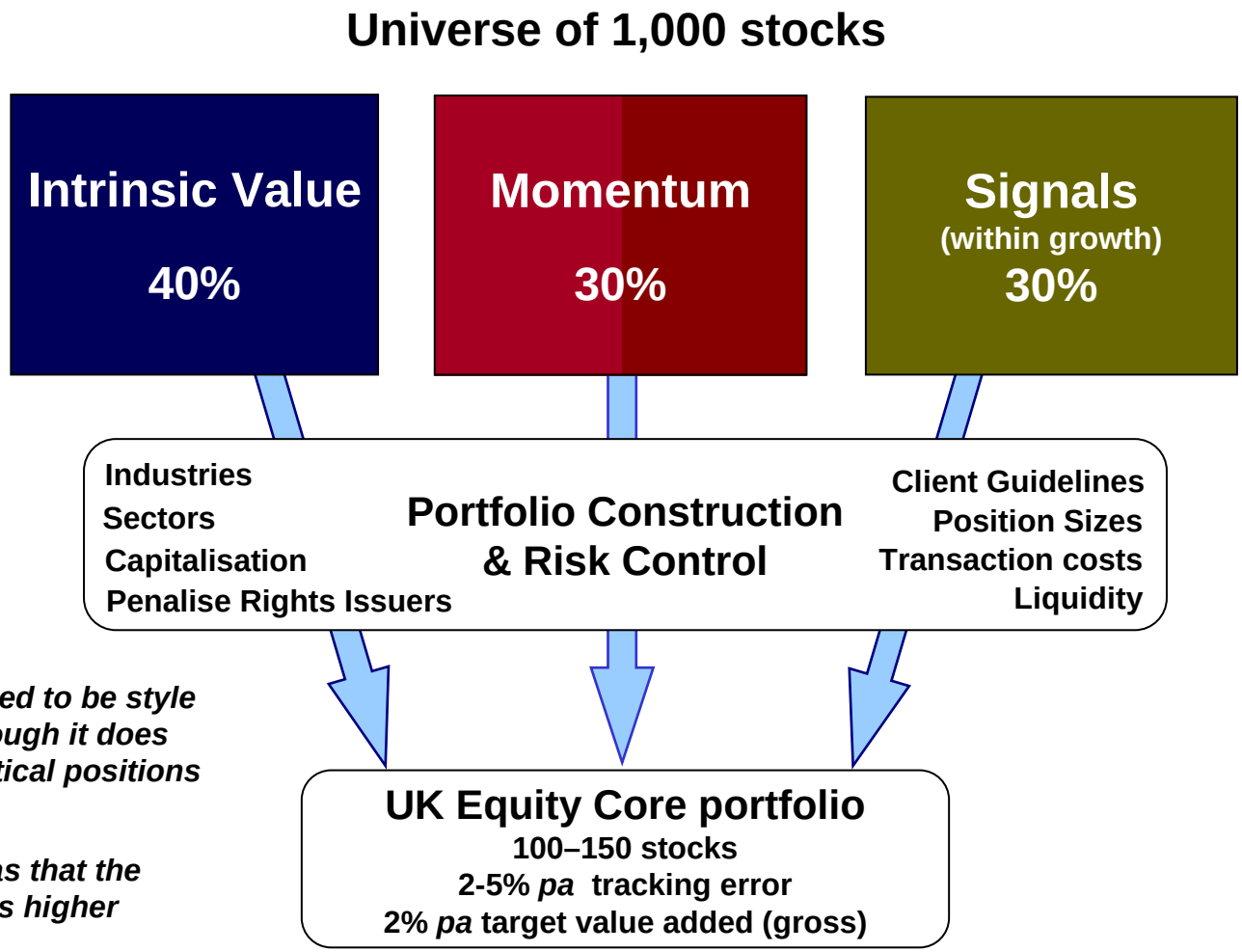
Note:
The FTSE World ex-UK is an unhedged index.

Performance data quoted represents past performance and is not predictive of future performance. Performance reflects the reinvestment of dividends and interest. Performance is net of investment management fees, fund expenses and other costs associated with the investment of the portfolio which are disclosed in the Fund Prospectus. Performance results are supplemental to the strategy's GIPS compliant presentation. A GIPS compliant presentation of composite performance has preceded this report in the past 12 months or accompanies this report, or is also available at www.gmo.com.

Investment Process Reminder

UK Equity Core Strategy

Implementation

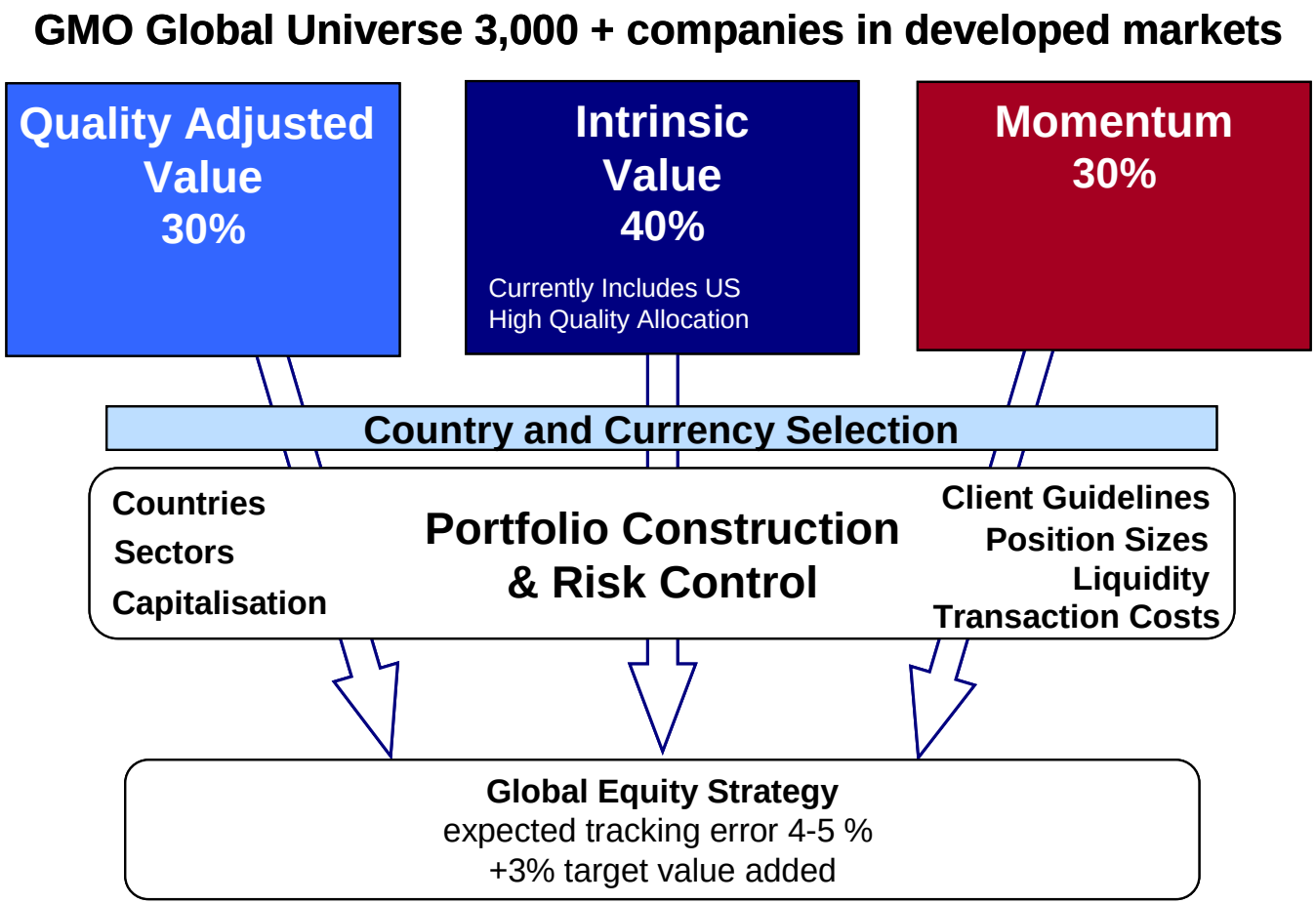


The strategy is designed to be style neutral over time although it does take opportunistic tactical positions where appropriate

The only long-term bias that the strategy has is towards higher quality stocks

Global Equity Strategy

Three diversifying approaches to stock selection



The strategy is designed to have a value bias.
An allocation to US High Quality stocks was introduced in Q1 2008.

As at end Dec 2009

Performance Review

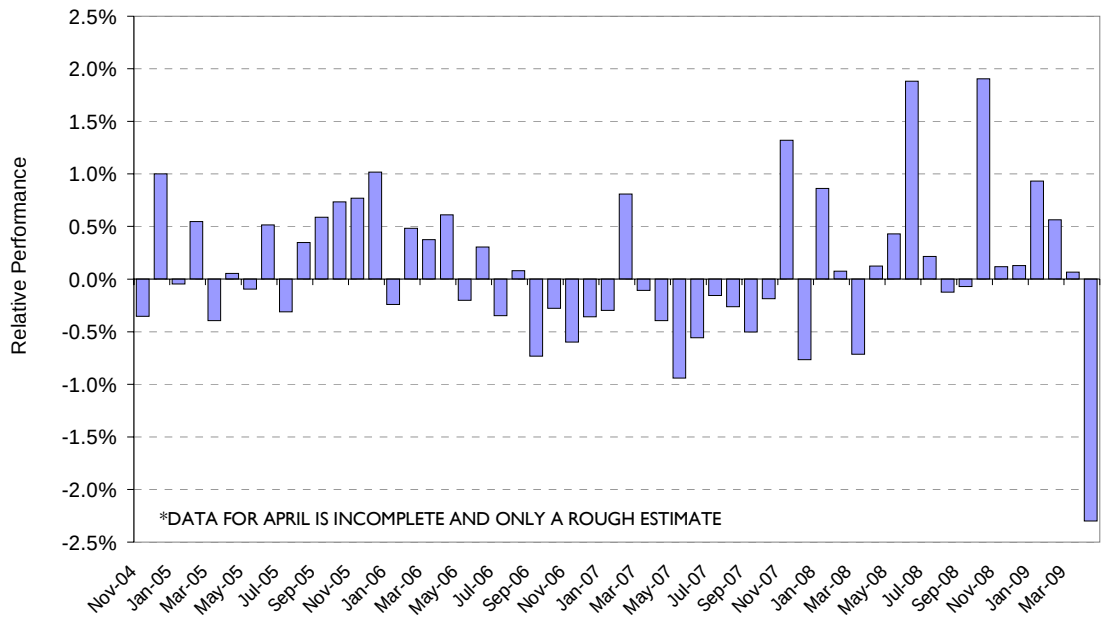
Up to 31st March 2010

Following On From Last Year's Presentation …

Slide taken from presentation to Shetland Islands Council, 27th May 2009

April* Will Probably Be The Strategy's Worst Month

UK Core Relative Returns (Nov 2004-Apr 2009)



Source: GMO
Data as at April 2009

GMO

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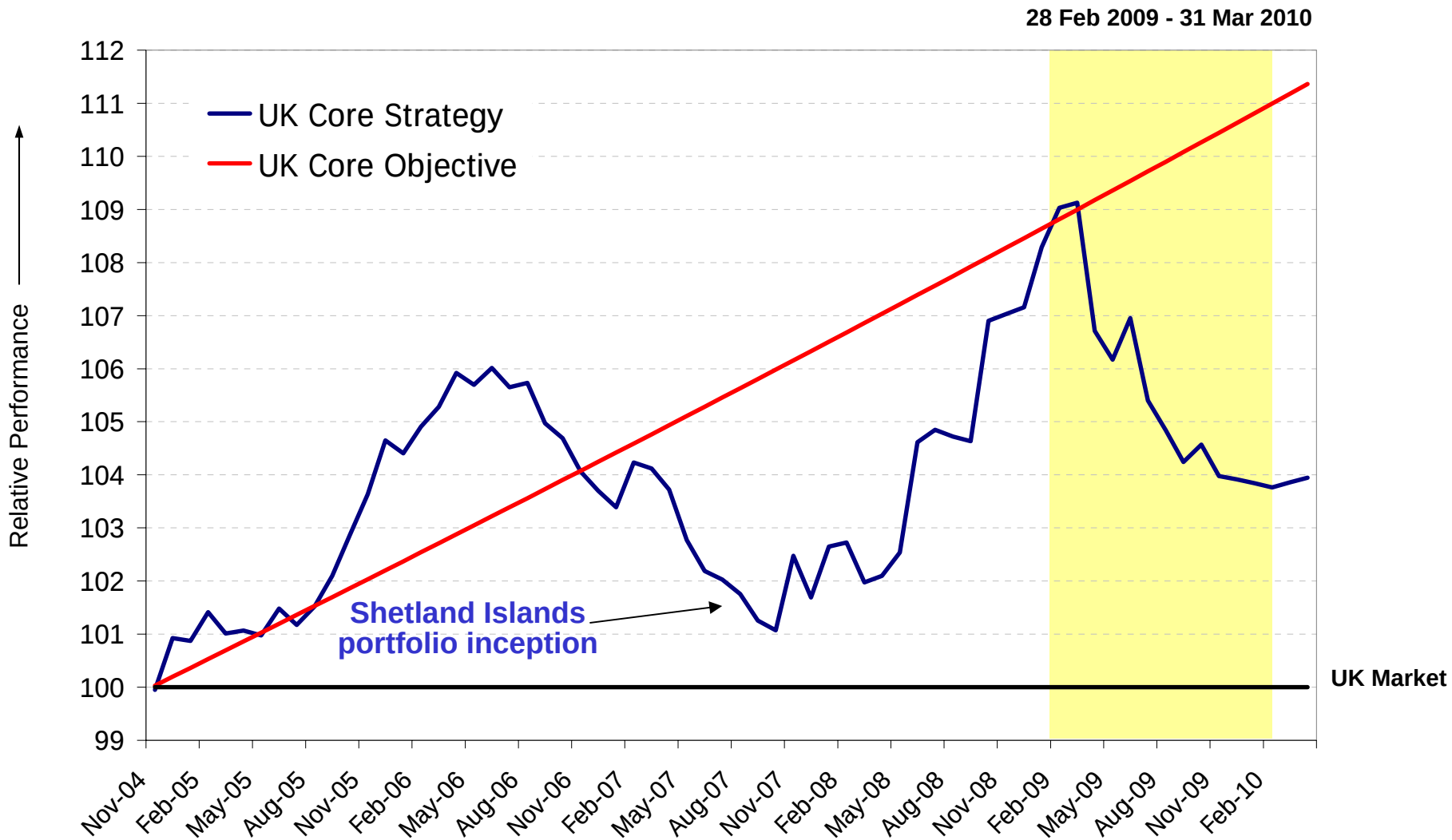
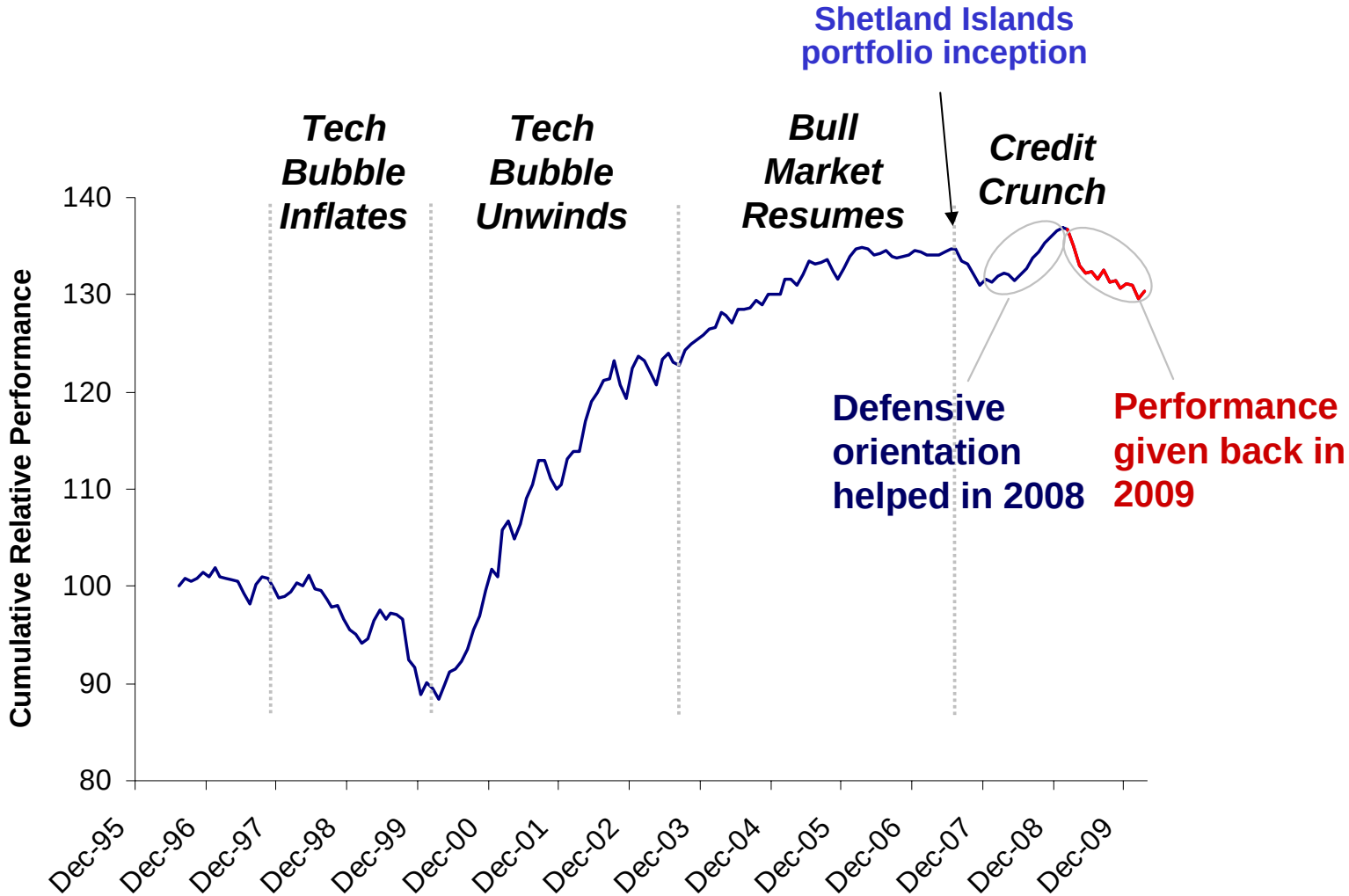
Performance Of UK Core Strategy & Objective



Data to end Apr 2010; returns are preliminary
Source: GMO

Performance Of GMO Global Equity Strategy

A tougher environment recently

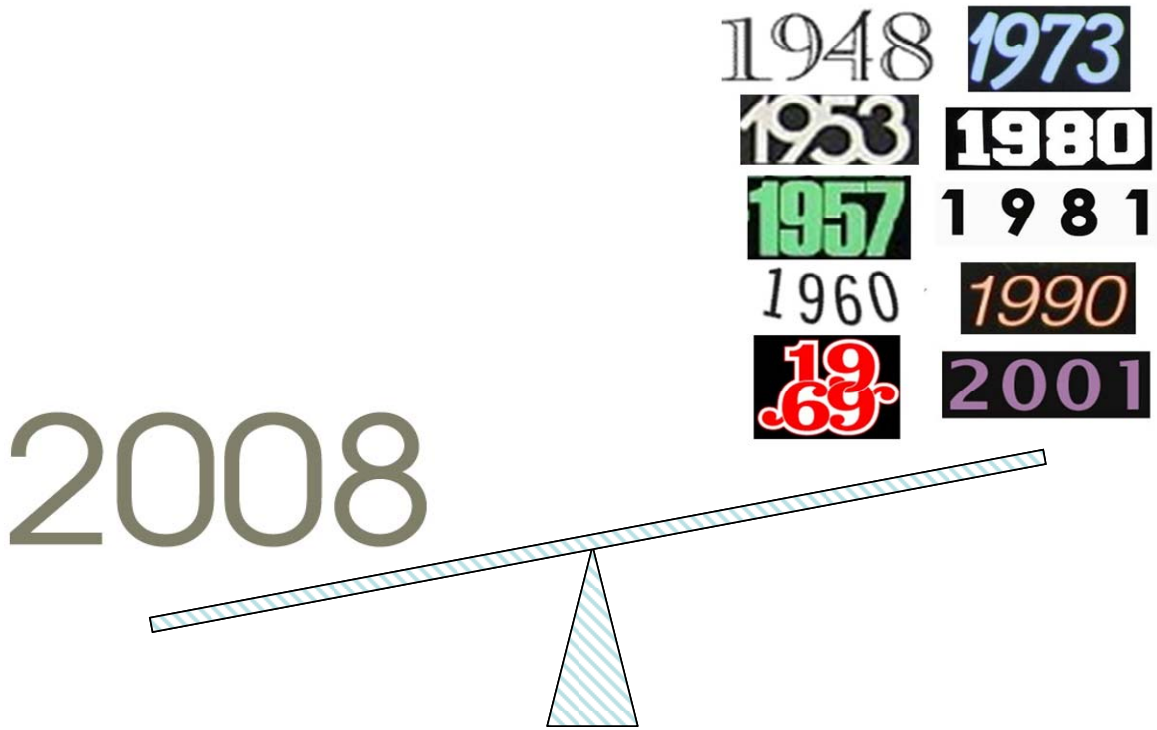


Performance presented gross of fees and expenses Performance is not indicative of future performance.
Please see performance disclosure on final page

Source: GMO
Data as at 31 Mar 2010

The Largest Government Stimulus In History

The US stimulus is bigger than all US post war stimuli COMBINED!



- There have been 11 post-war recessions in the US
- The current recession has prompted an unprecedented government response

Source: GMO, Grant's Interest Rate Observer, April 2009

Phases Of The Market Through 2009 And 2010

The powerful rally from March to May was the most notable feature of the period

2009 | **2010**

Jan-Feb

More 2008

"Markets remain in fear mode"

FTSE-All falls 12.0%

MSCI World falls 25%

March-May

A Mighty Sigh of Relief

"The government backstop worked"

FTSE-All Share rises 18.3% in 3 months

MSCI World rises 45%

June-Dec

Measured Rises

"The worst has passed, but risk hasn't disappeared"

FTSE-All Share rises 24.9% in 7 months

MSCI World rises 17%

Jan-Mar

Similar Weather

"Markets continue to focus on the positives"

FTSE-All rises 6.4%

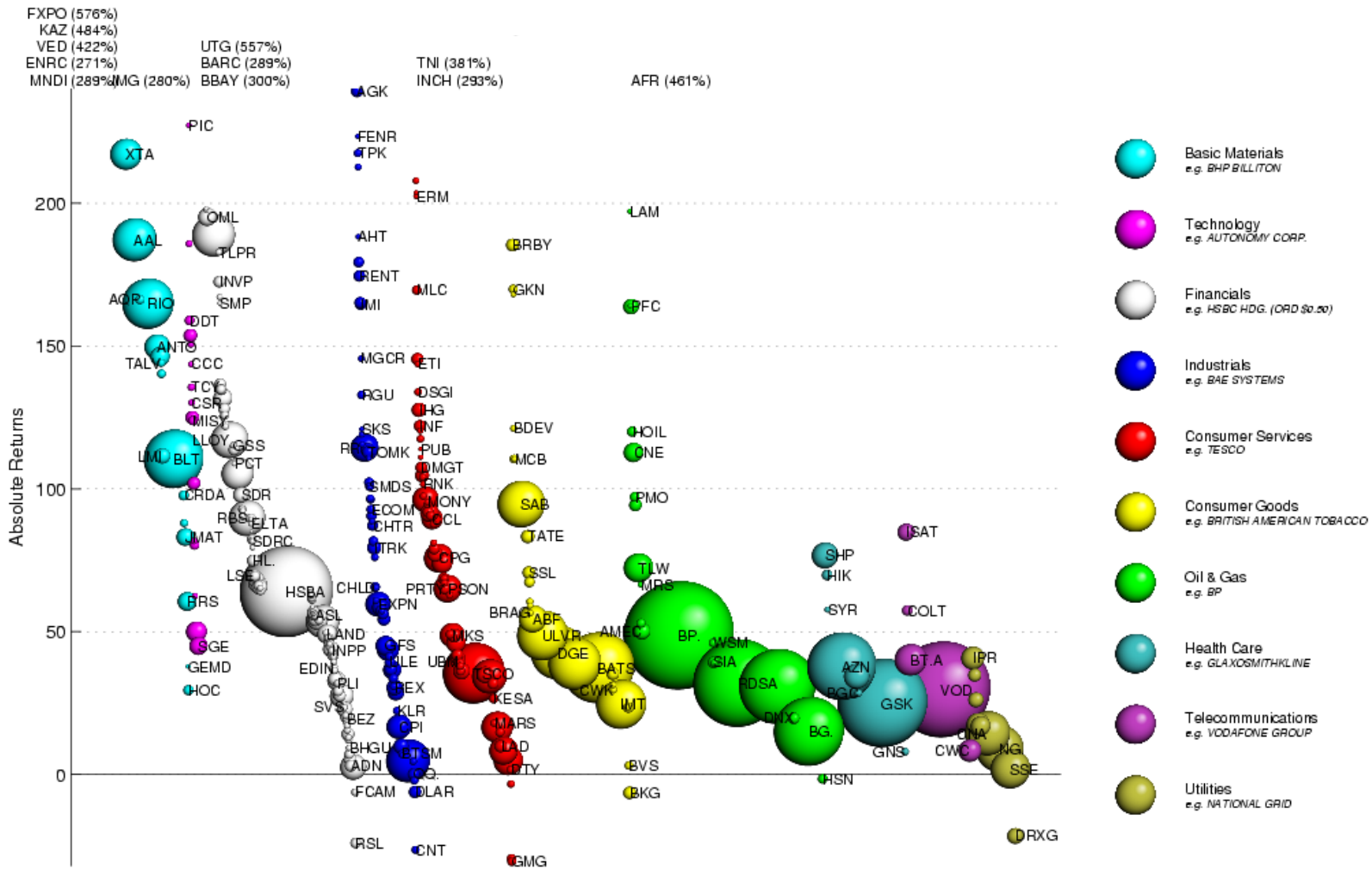
MSCI World rises 3%

FTSE-All Share rose 58% over this period

Source: FTSE, MSCI, GMO
Data as at end Mar 2010

Which Stocks Drove The UK Market Higher?

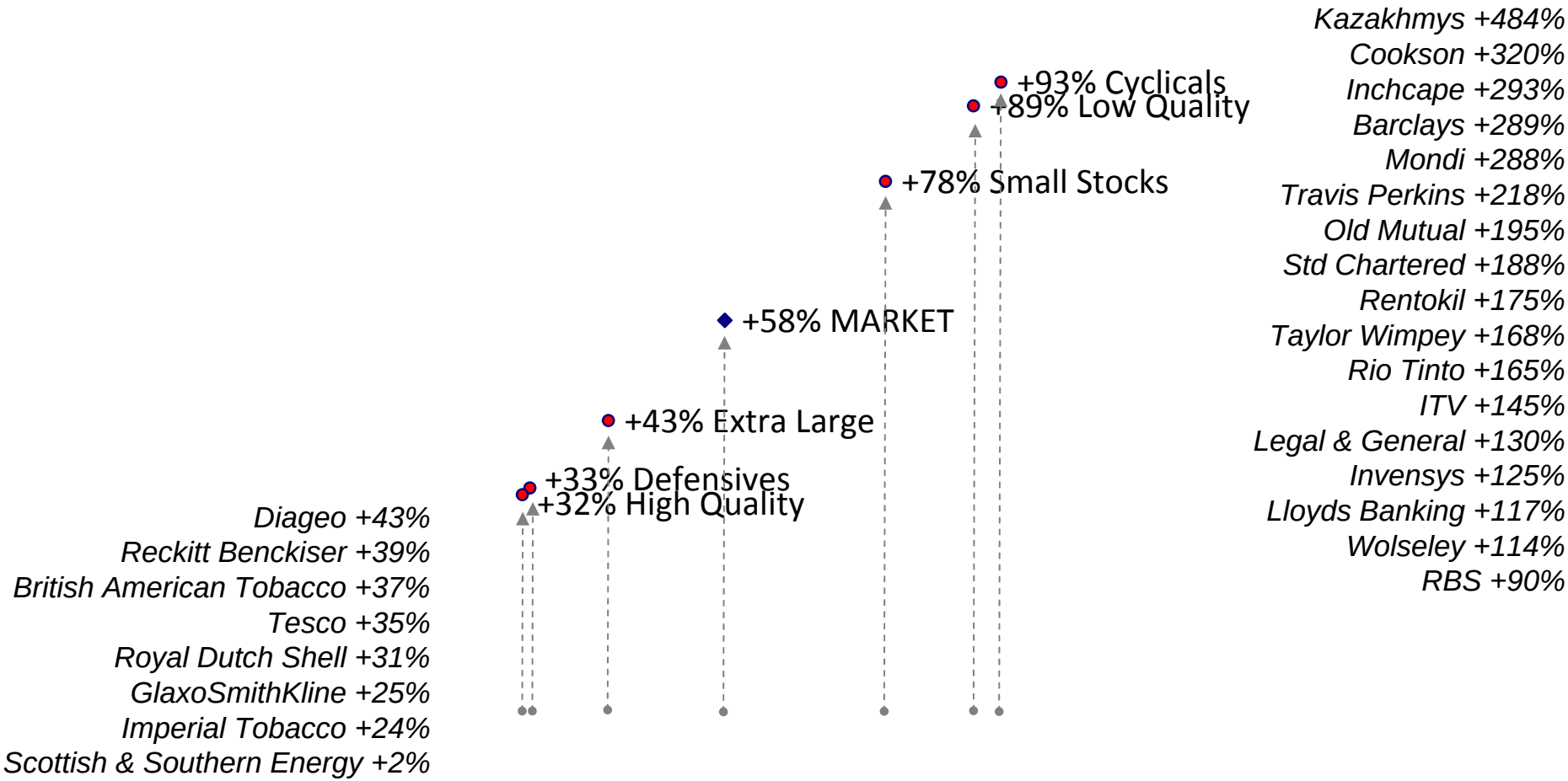
UK Stock Market Constituent Returns for 28 Feb 2009 to 31 Mar 2010



Source: GMO
Data as at 31 March 2010

It Was All About Quality ...
The Lower The Quality, The Higher The Return

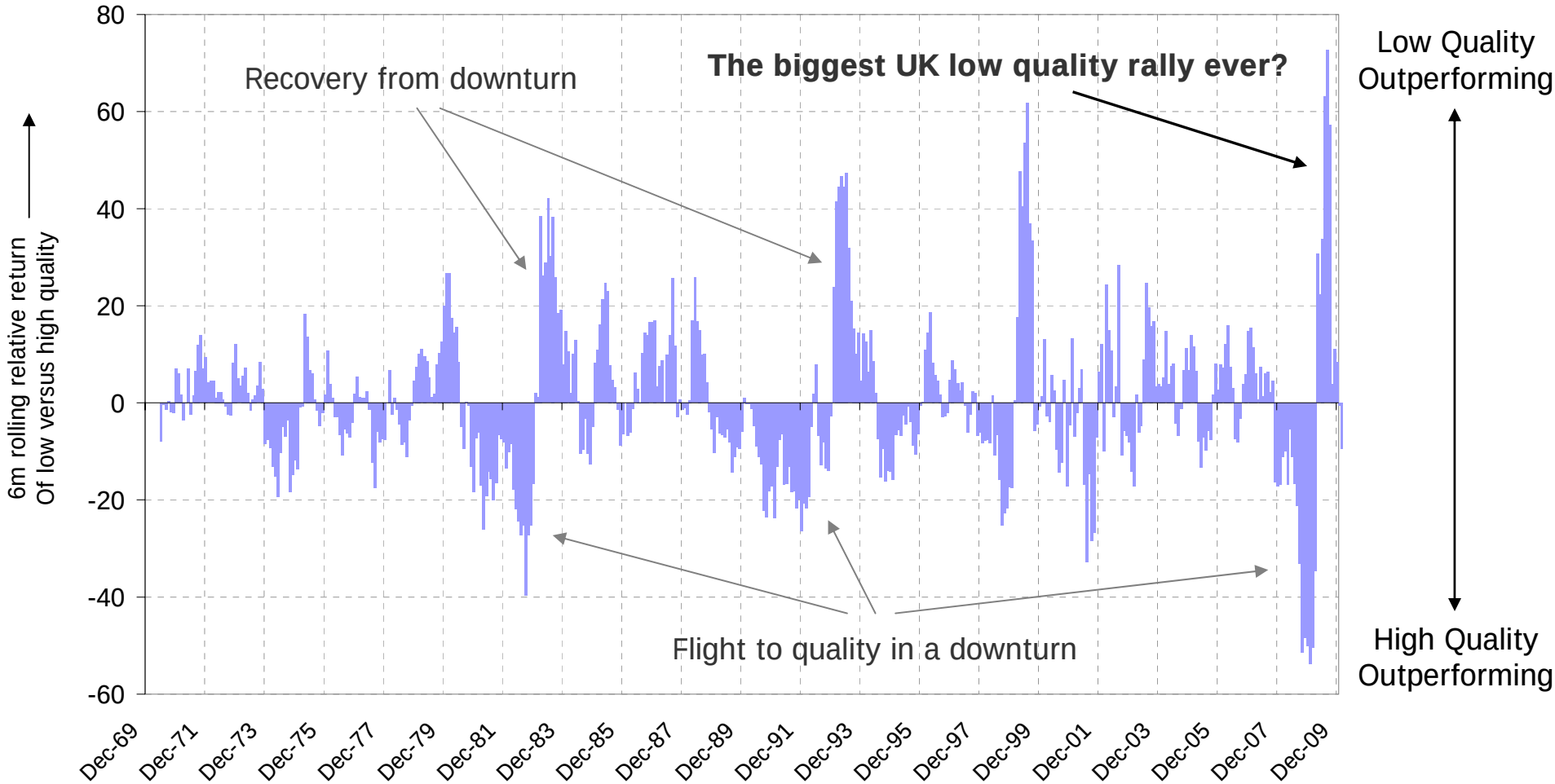
UK Stock Market Constituent Returns
(28 Feb 2009 to 31 Mar 2010)



Source: GMO
Data as at 31 March 2010

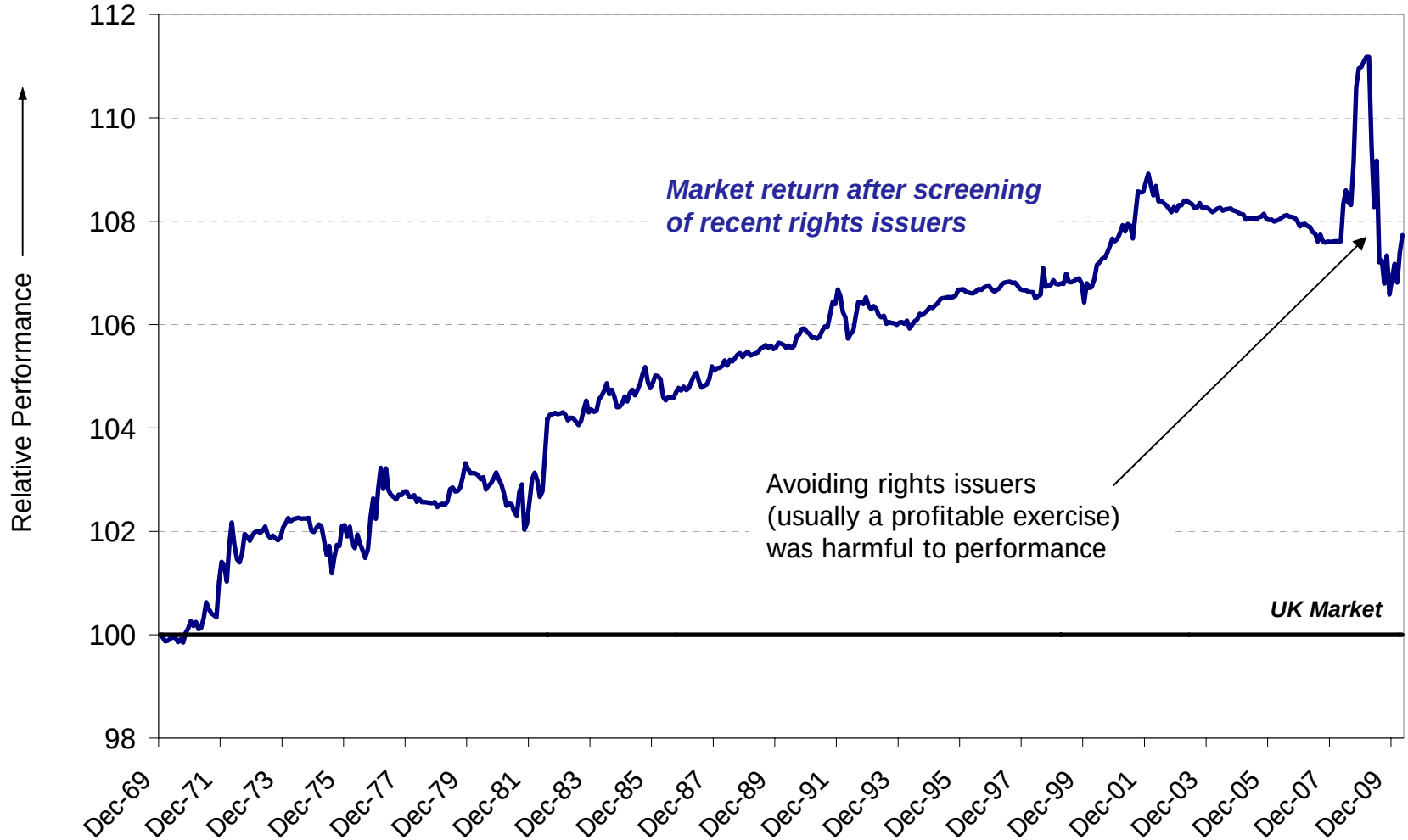
Putting Things Into Historic Context

Six month relative return of lowest 20% quality versus highest 20% quality in the UK



Source: GMO
Data as at 31 Dec 2010

Even UK Rights Issuers Outperformed

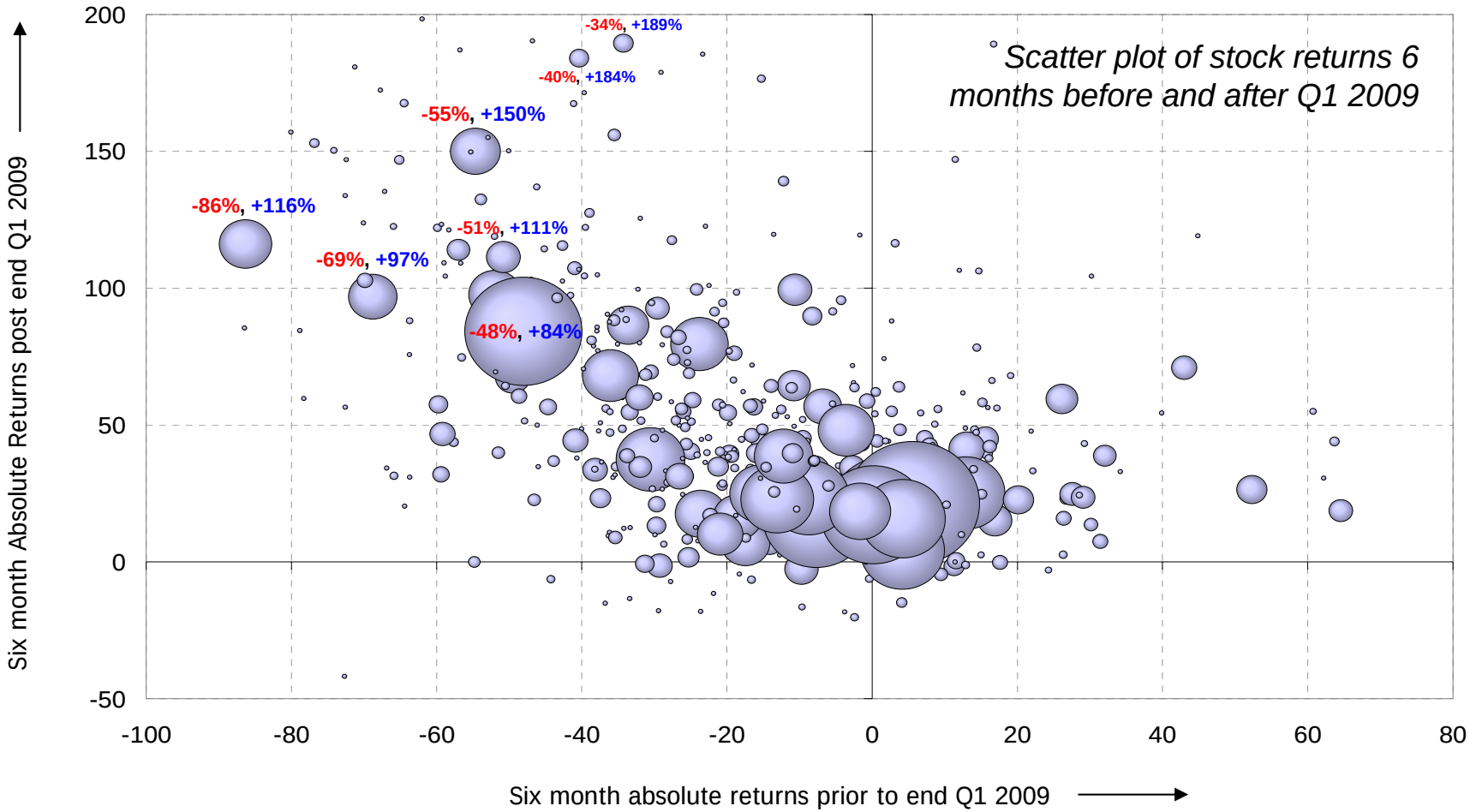


Note: Performance data quoted represents past performance and is not indicative of future results

Source: GMO
Data as at 31 Mar 2010

The Other Extreme Event Was The Turnaround!

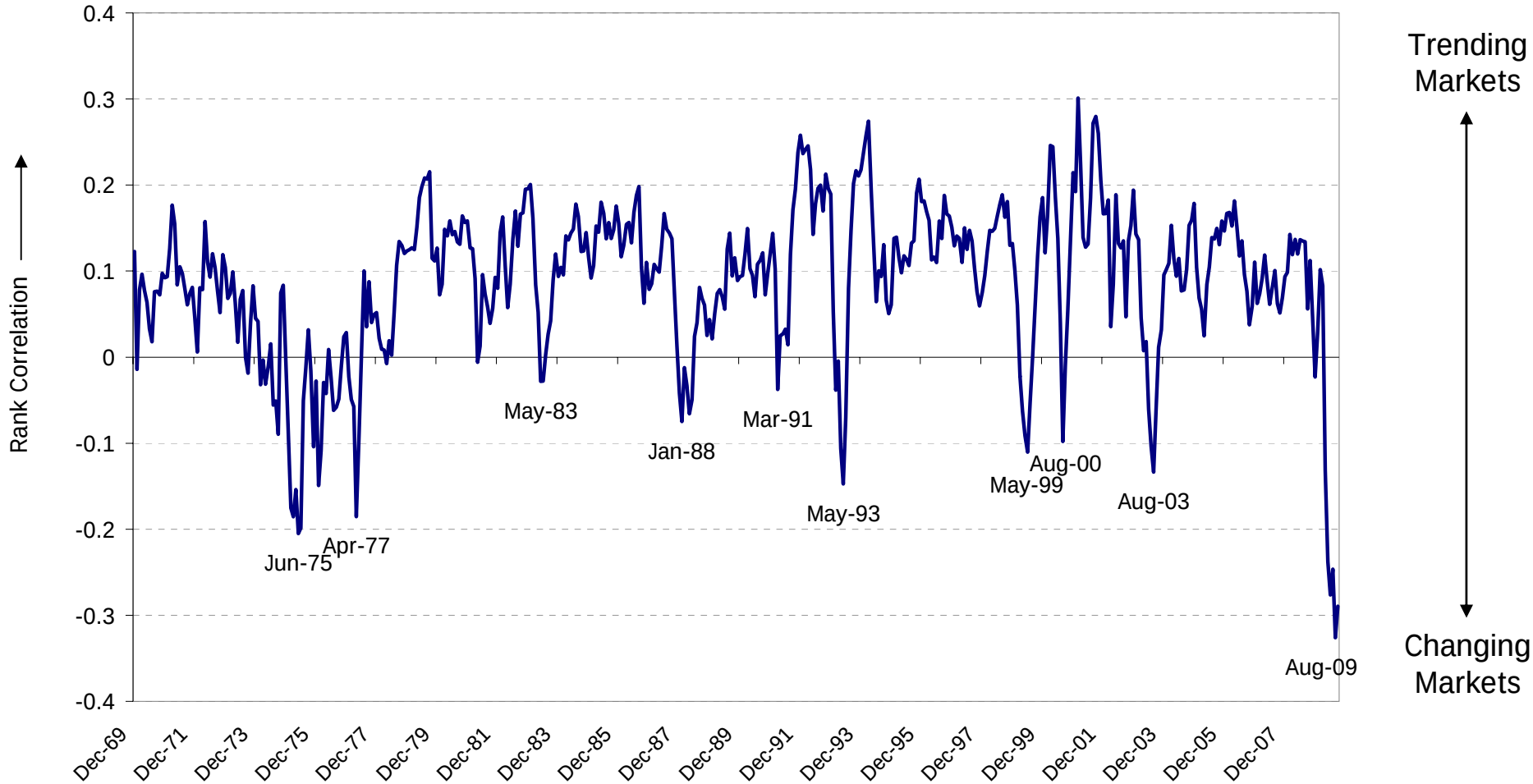
What Went Down Then Goes Up!



Source: GMO
Data on UK Equities. As at Sept 2009

The Biggest Turnaround We Have Ever Witnessed

Rank correlation of six month apart six month return ranks in the UK

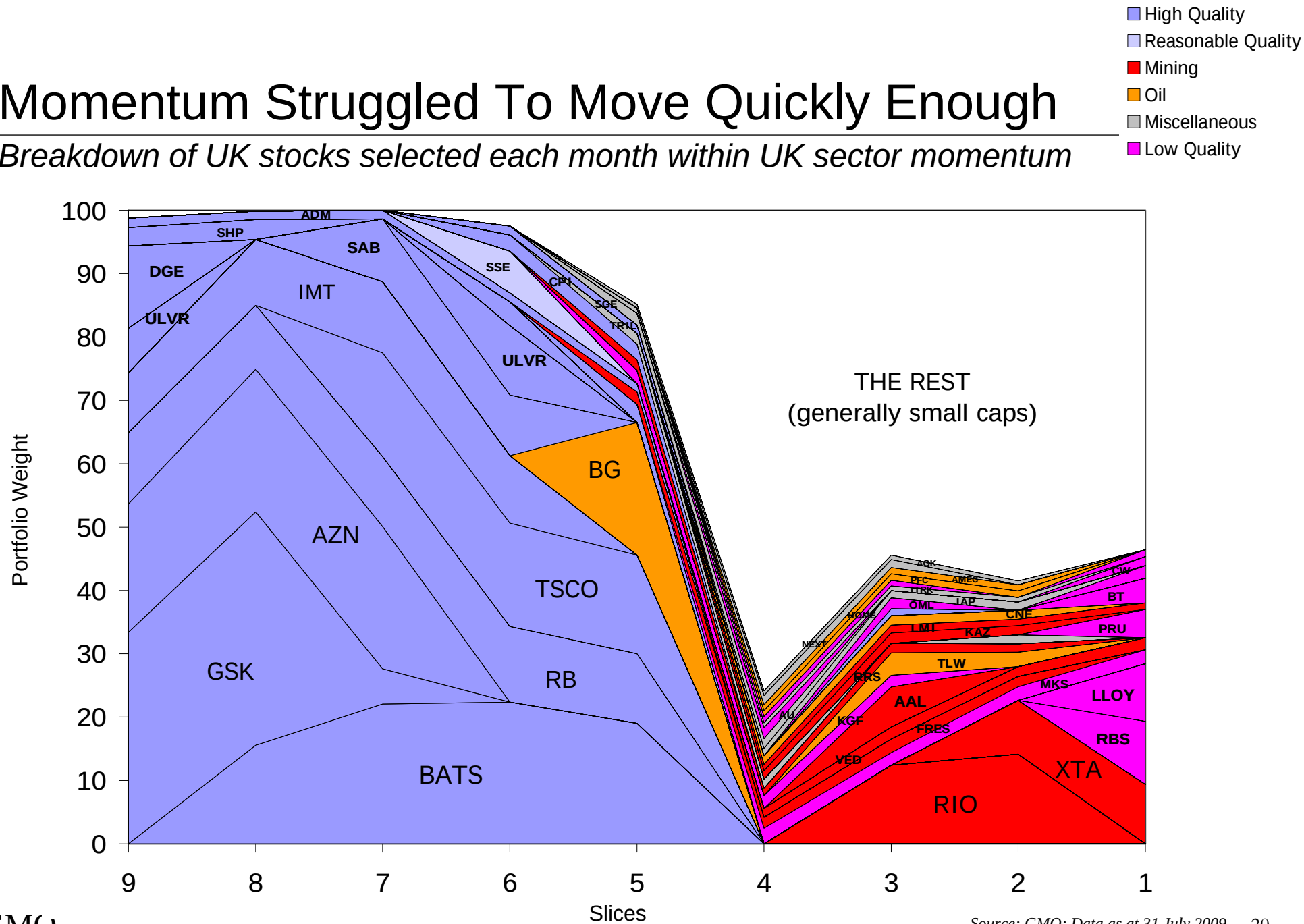


Source: GMO

Data on UK Equities; as at Sept 2009

Momentum Struggled To Move Quickly Enough

Breakdown of UK stocks selected each month within UK sector momentum

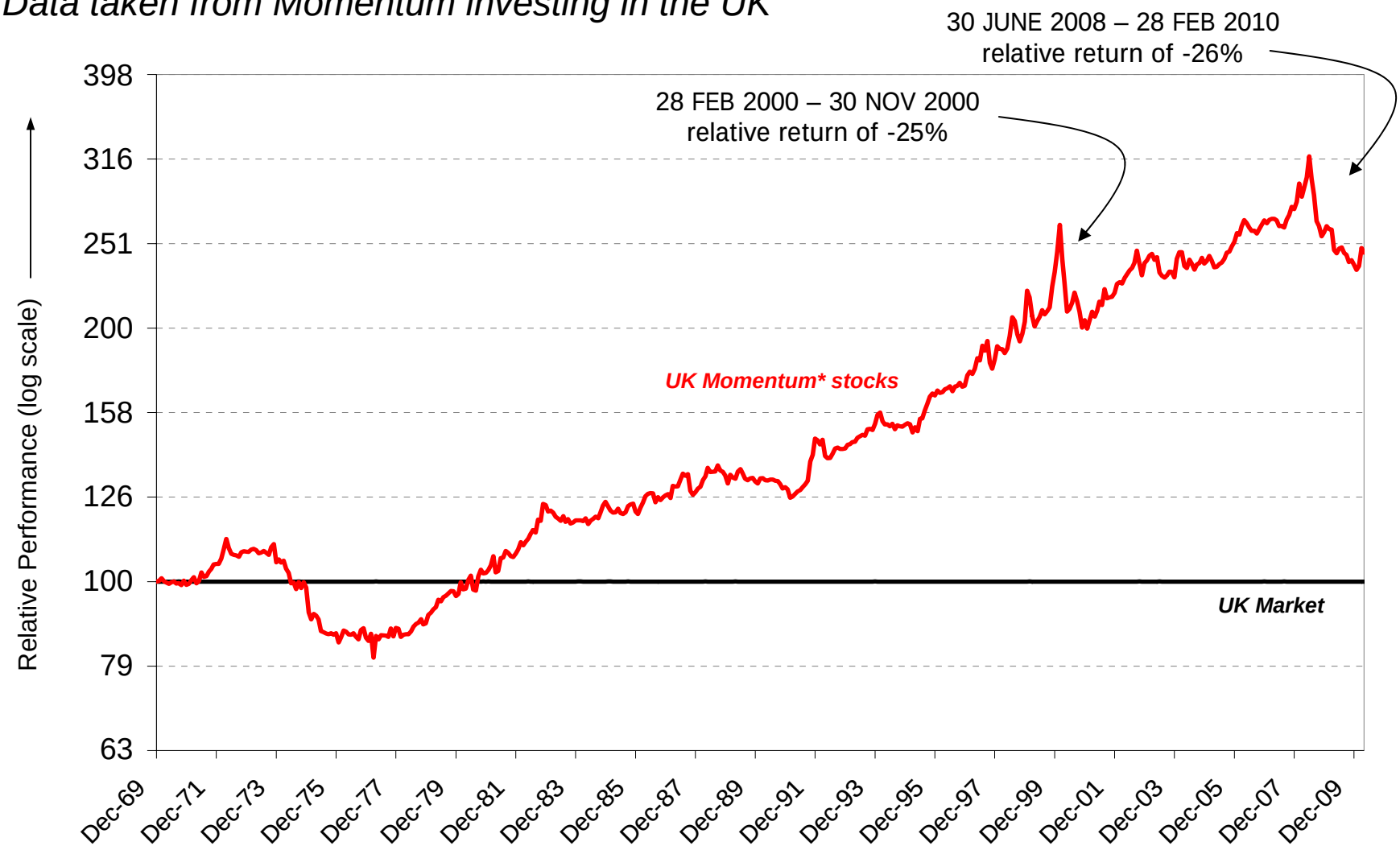


Source: GMO; Data as at 31 July 2009

GMO

Momentum Has Performed Poorly Recently

Data taken from Momentum investing in the UK

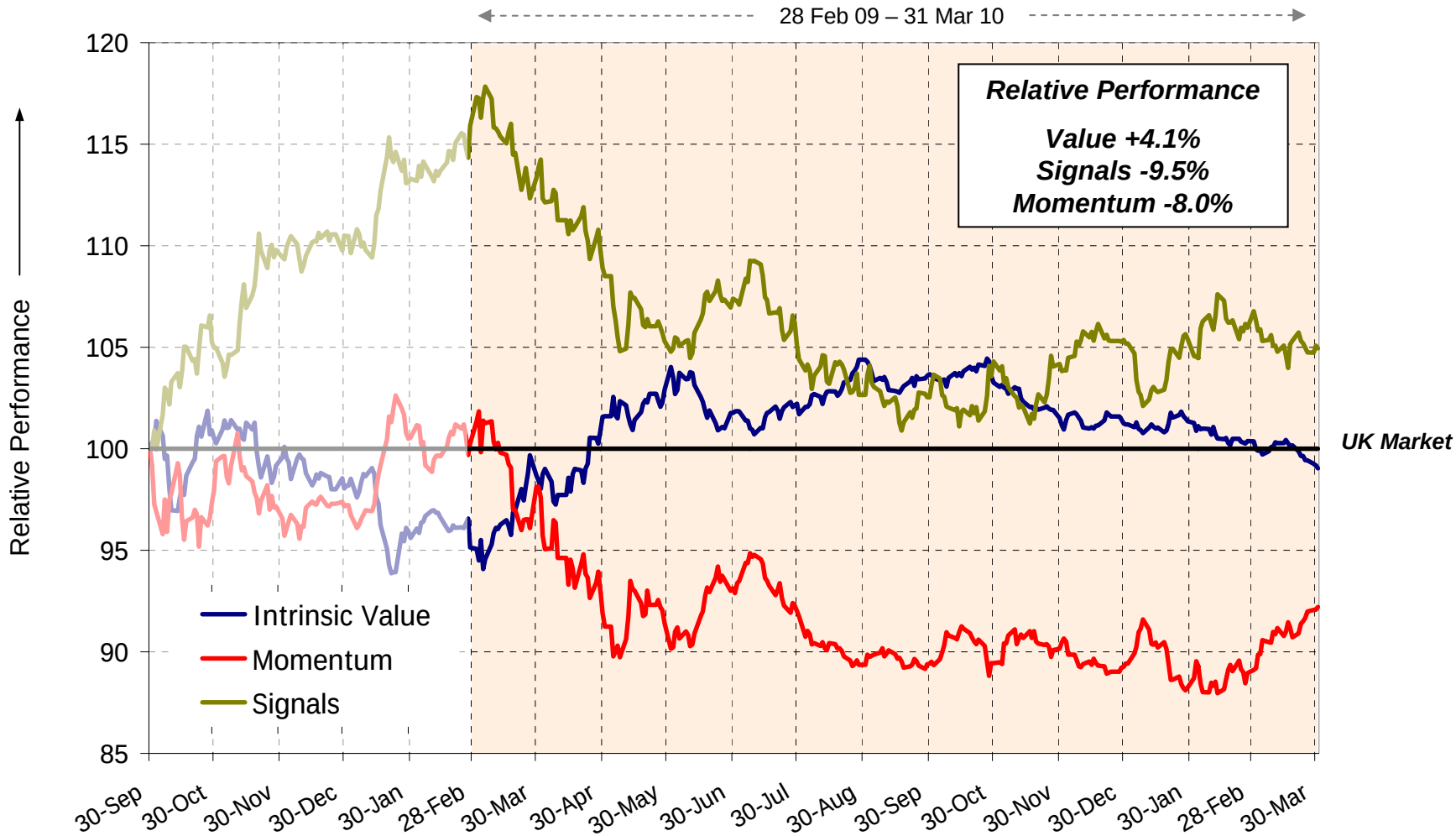


***Note**: Performance data quoted represents past performance and is not indicative of future results*
**Momentum is defined here as best 15% (by market cap) trailing six month price return using market cap weighting sliced 9 months*

Source: GMO
Data as at 30 Apr 2010

Performance Of The UK Stock Selection Techniques

Signals and Momentum performed poorly while Value outperformed



***Note**: Performance data quoted represents past performance and is not indicative of future results.*
Assumes no transaction costs; excludes impact of cash holdings; data to 31 March 2010

Source: GMO

Performance Of The Non-UK Stock Selection Techniques

Your portfolio was too defensive for 2009

Relative Performance

QAV +3.5%
Non US IV +0.3%
US HQ -6.4%
Momentum -10.4%

GMO World ex-UK Equity Fund - Approximated performance of sub-portfolios

Approximated performance is calculated assuming instantaneous trading without transaction costs, fees or cash flows.

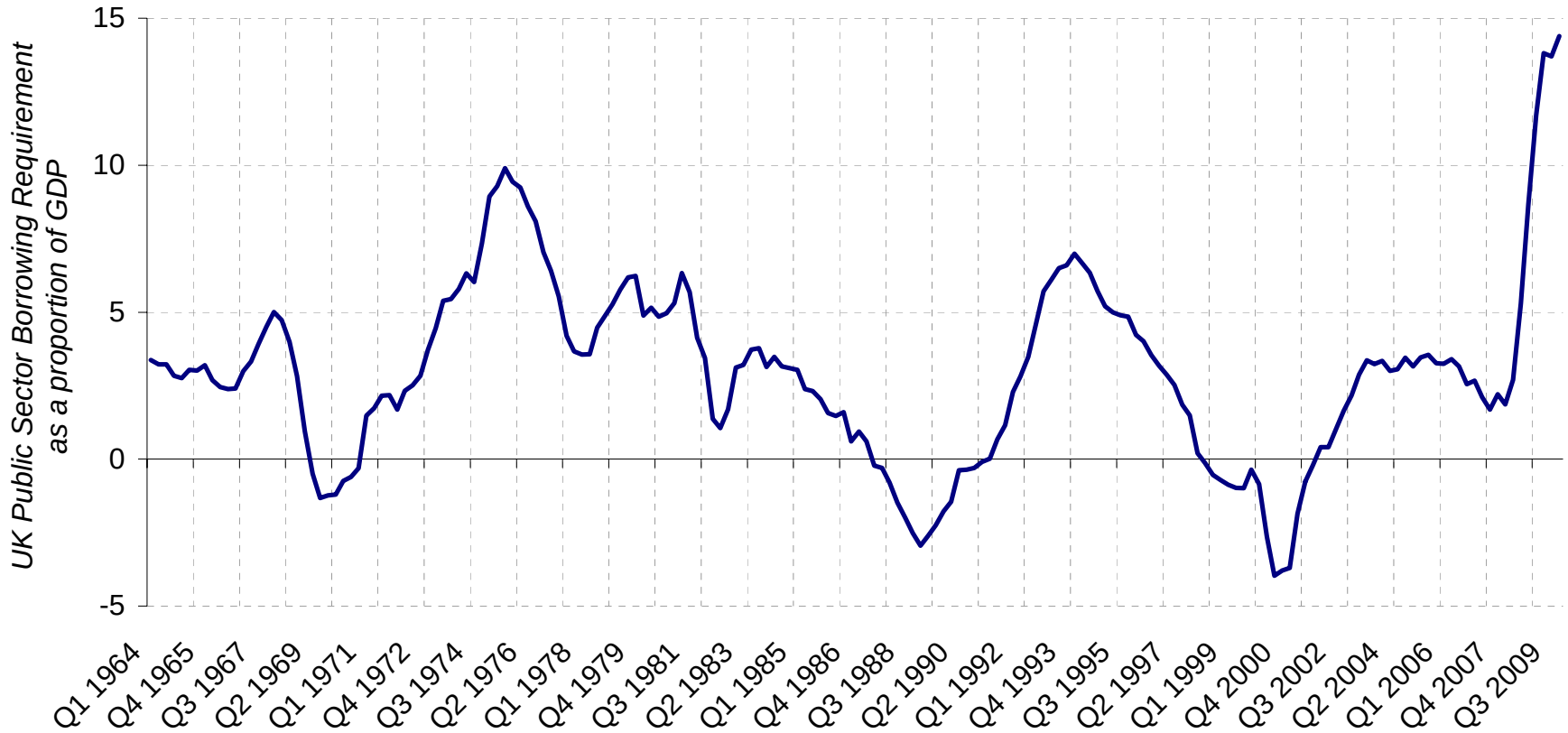
Data as at 31/03/10
Source: GMO

Outlook And Portfolio Positioning

UK Equities

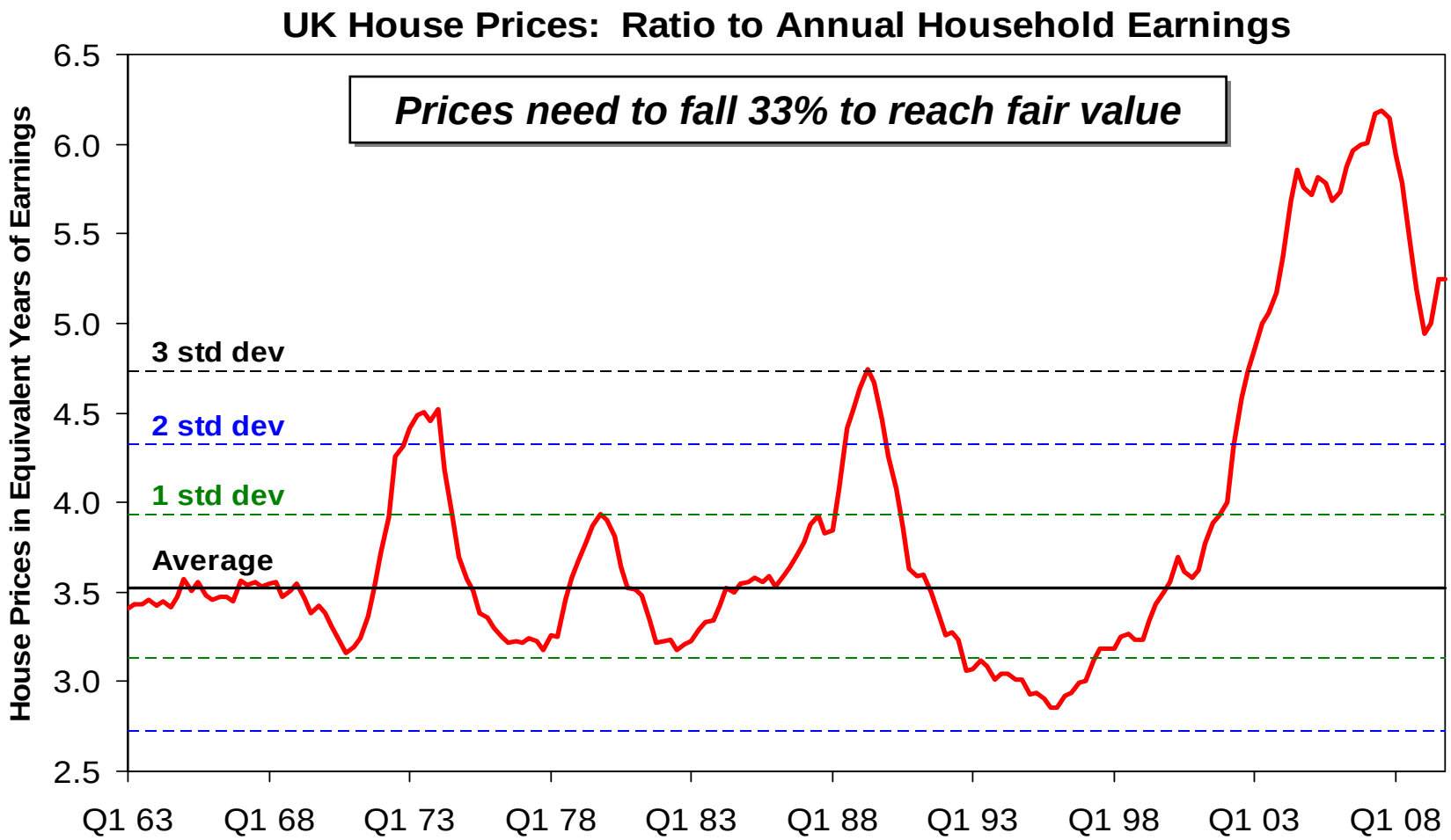
We Are Not Out Of The Woods Yet!

UK Public Sector Borrowing Requirement as a proportion of GDP



Source: Datastream, GMO
Data as at 31 Mar 2010

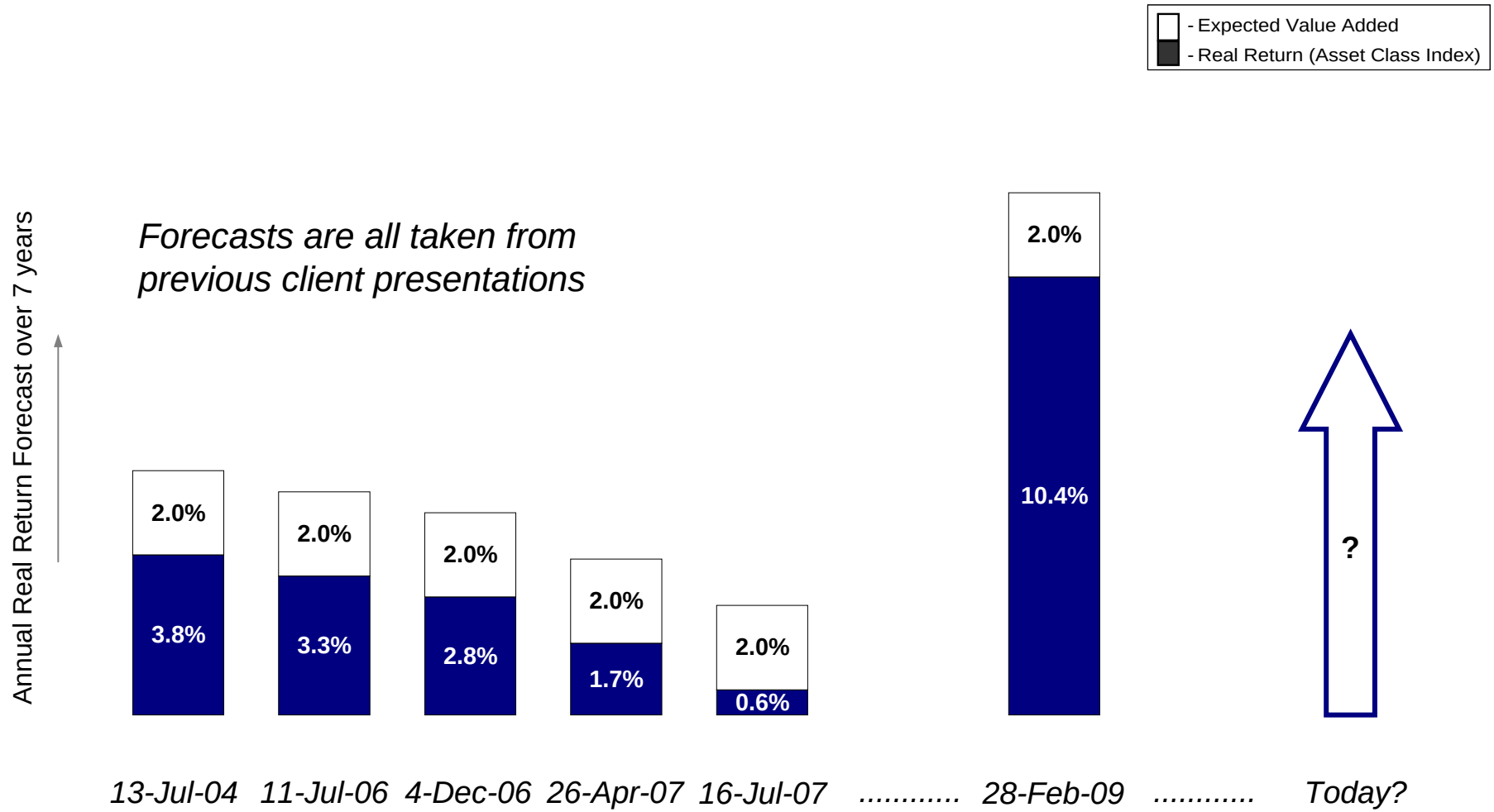
UK Housing Bubble Has Yet To Correct



Source: Datastream, GMO
Data as at 31 Dec 2009

A Comment On The Level Of The Overall Market

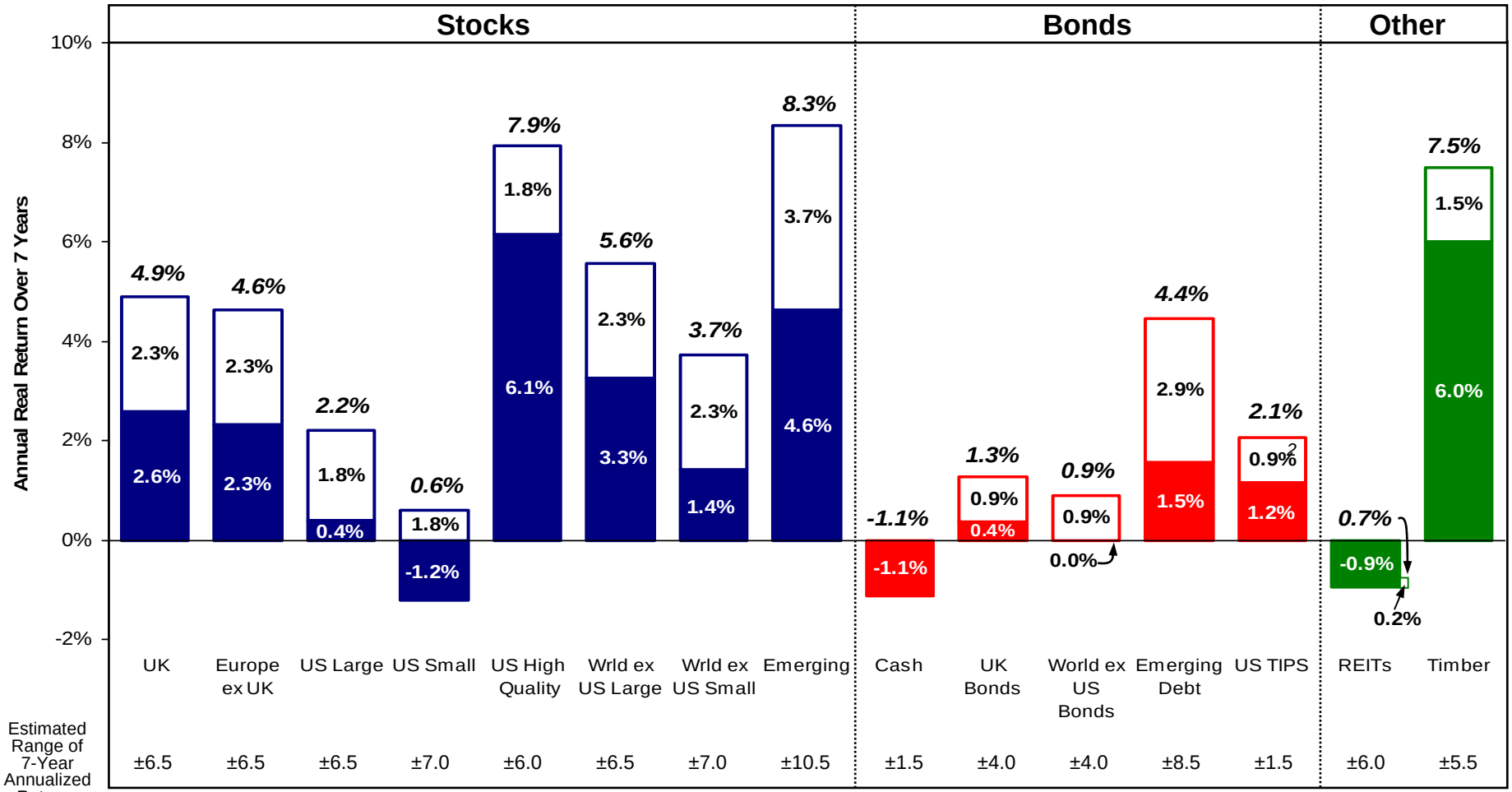
Previous GMO 7 year real return forecasts (2004-2009)



Source: GMO

GMO 7 Year Asset Return Forecasts*

As at 31 March 2010



***The chart represents real return forecasts[1] for several asset classes and an estimate of value expected to be added from active management. These forecasts are forward-looking statements based upon the reasonable beliefs of GMO and are not a guarantee of future performance.**

[1] Long-term inflation assumption: 2.8% per year.

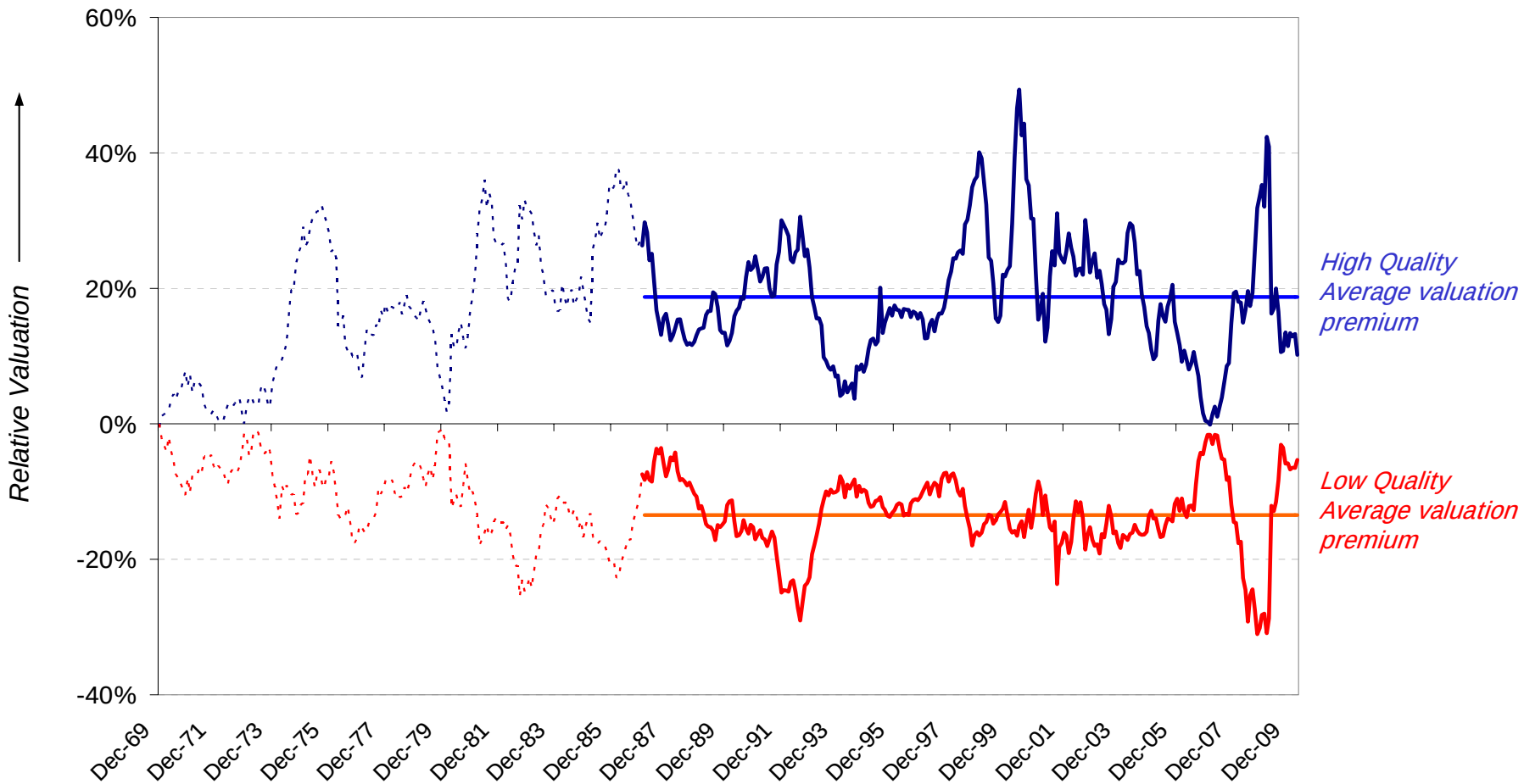
[2] Alpha transported from management of global bonds.

GMO

Source: GMO

Low Quality Stocks Look Expensive

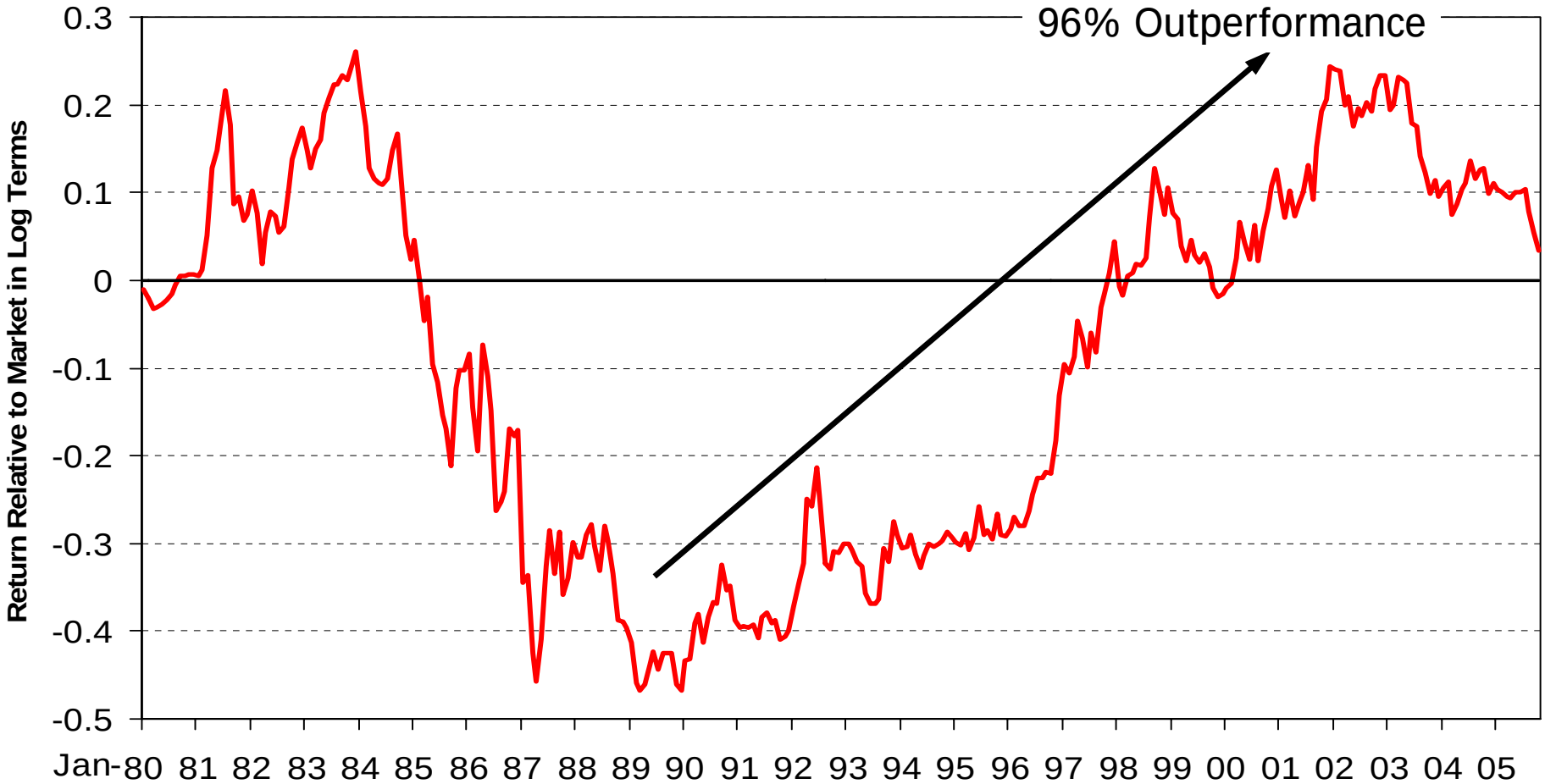
Valuation of Quality stocks in the UK*



**Valuation uses Price to Scale (pre quality adjusted QAV) methodology*
Quality stocks are defined as best/worst 30% using market cap weighting sliced 12 months

As at 31 Mar 2010
Source: GMO

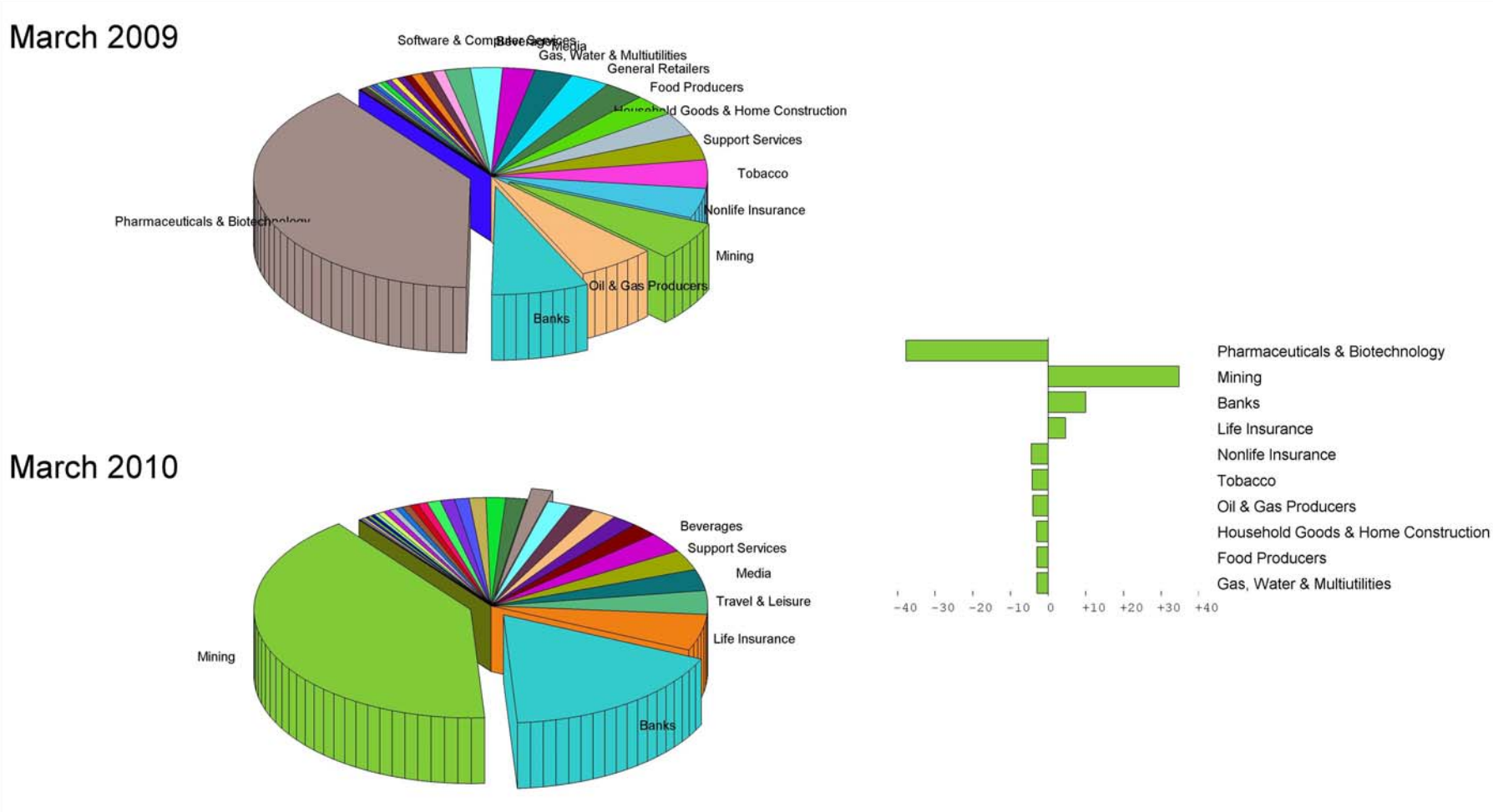
Quality Performed Very Well During Japan's Bust



Source: GMO, MSCI As of 10/31/2005

Momentum Is Currently The Odd One Out

Composition of UK Sector Momentum Portfolios



Source: GMO data to 31 Mar 2010

Outlook And Portfolio Positioning

World Ex-UK Equities

Current Opportunities In Global Equities

A more broadly based set of positions than a year ago

US High Quality

Momentum

"Traditional" Value

Pharma

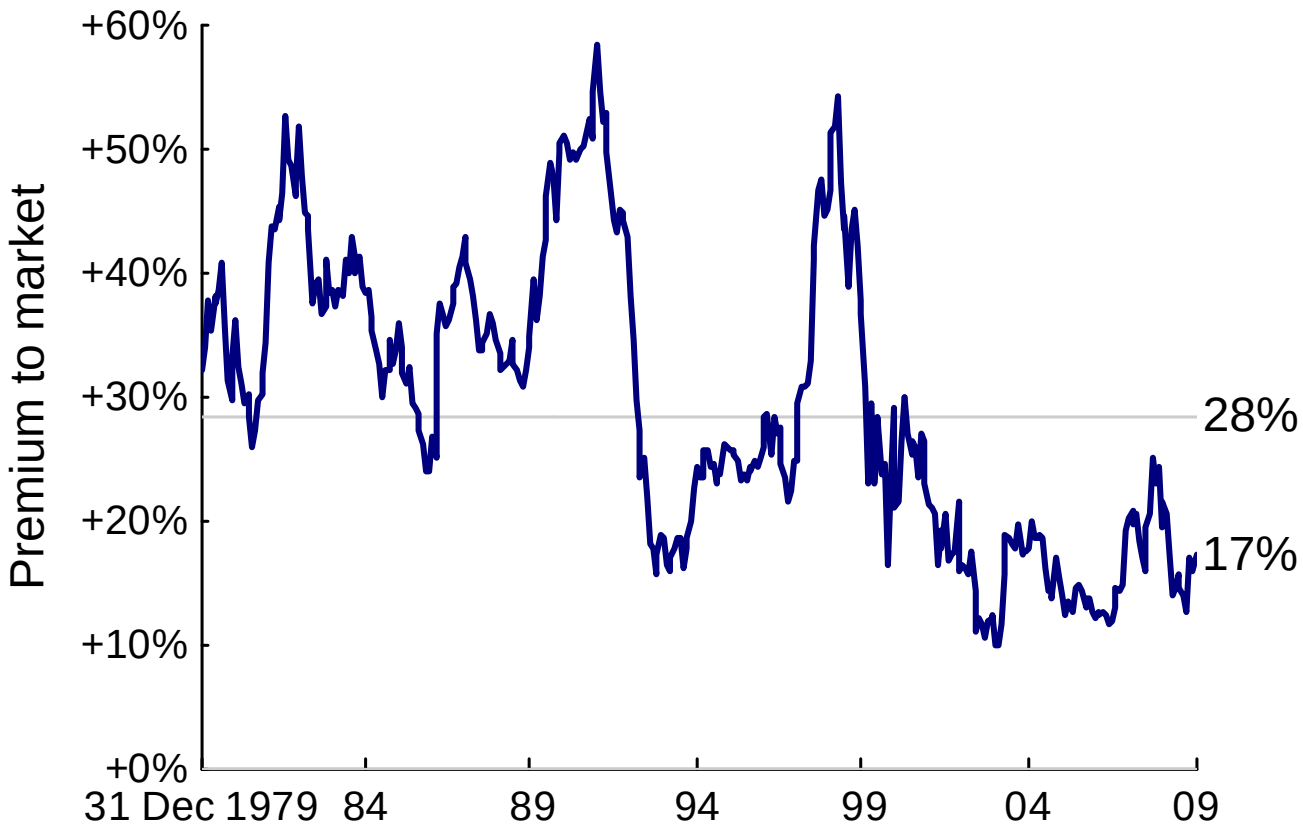
	Total
JOHNSON & JOHNSON	3.7
APPLE INC	2.3
MERCK & CO	2.0
COCA-COLA CO	1.9
WAL-MART STORES INC	1.8
PEPSICO INC	1.5
GOOGLE INC	1.5
BNP PARIBAS	1.5
ENI	1.4
PFIZER INC	1.3
TOTAL	1.1
ABBOTT LABORATORIES	1.1
3M CO	0.9
NISSAN MOTOR CO	0.9
UNICREDIT ORD	0.8

GMO World ex-UK Equity Fund
Portfolio holdings are subject to change and should not be considered a recommendation to buy individual securities

Data as at 31/03/10
Source: GMO

Relative Valuation Of High Quality Companies In US

US blue-chips trade at attractive prices again



- High quality stocks typically trade at a c.28% premium to the market on this measure
- They got close to normal levels earlier in the year but never made it
- Today they trade substantially below normal levels
- According to our estimates, a return to normal levels would deliver 5%+ p.a. ahead of the broader market for 7 years

Chart shows the relative valuation of the highest quality 10% of the US market as measured by GMO composite value.
GMO defines quality companies as those with high profitability, low profit volatility, and minimal use of leverage.
Source: GMO Data as at December 2009

A Comparison Of Two US Food & Beverage Companies

You can buy shares in Coca-Cola at the same price as weaker peers

	Tyson	Coca-Cola	
Profitability (Return on Equity)	4.5%	26%	Coca-Cola is higher quality
Debt levels (Debt / Equity)	77%	21%	
Valuation (Price to Earnings[1])	21x	21.5x	Both stocks trade on similar valuations. Buy the better quality one!

1. Using "Normalized" Earnings

Source: GMO
Data as at end Dec 2009

Relative Valuation Of Value Stocks

Current "traditional" value opportunities are reasonably priced

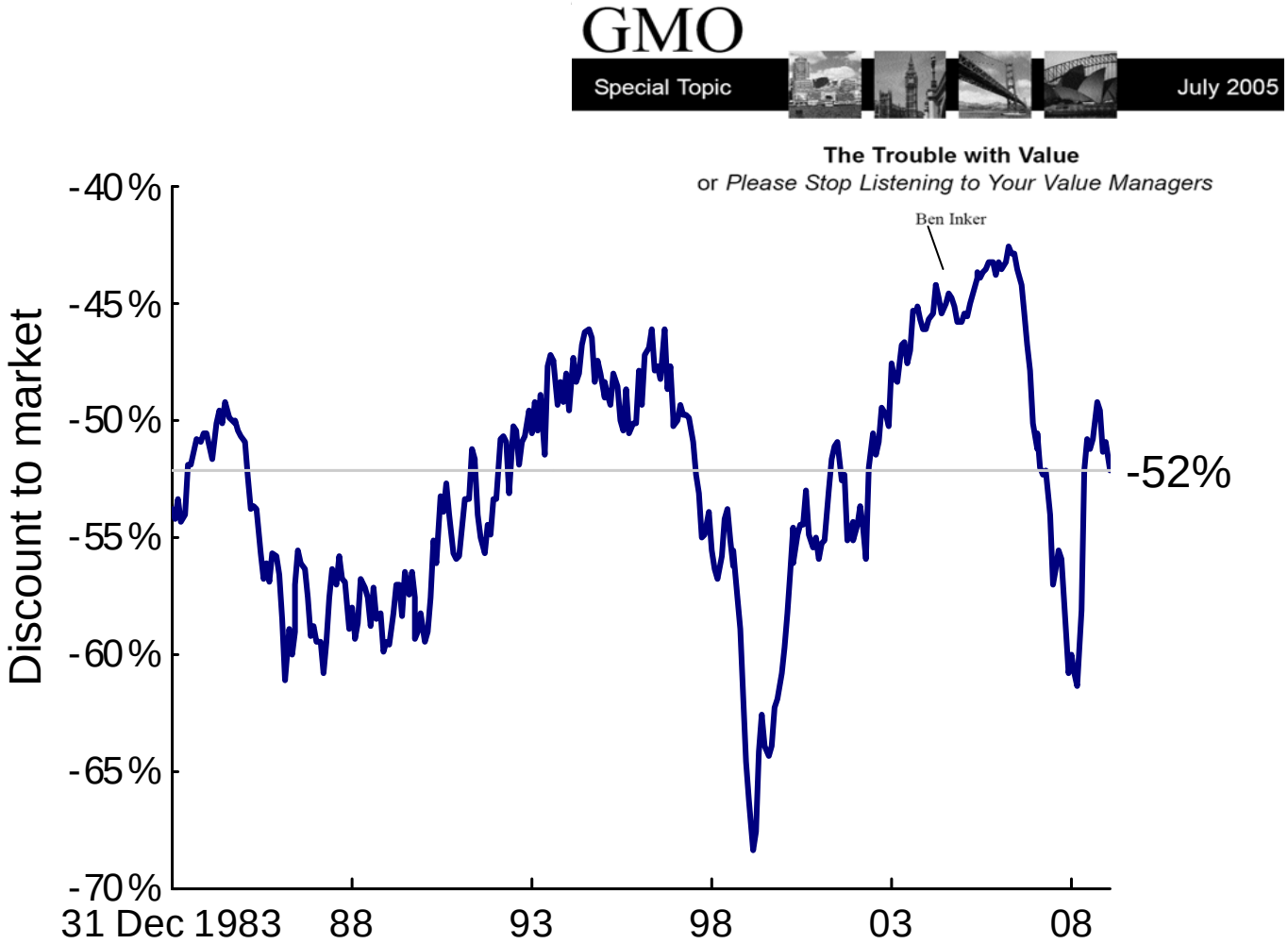
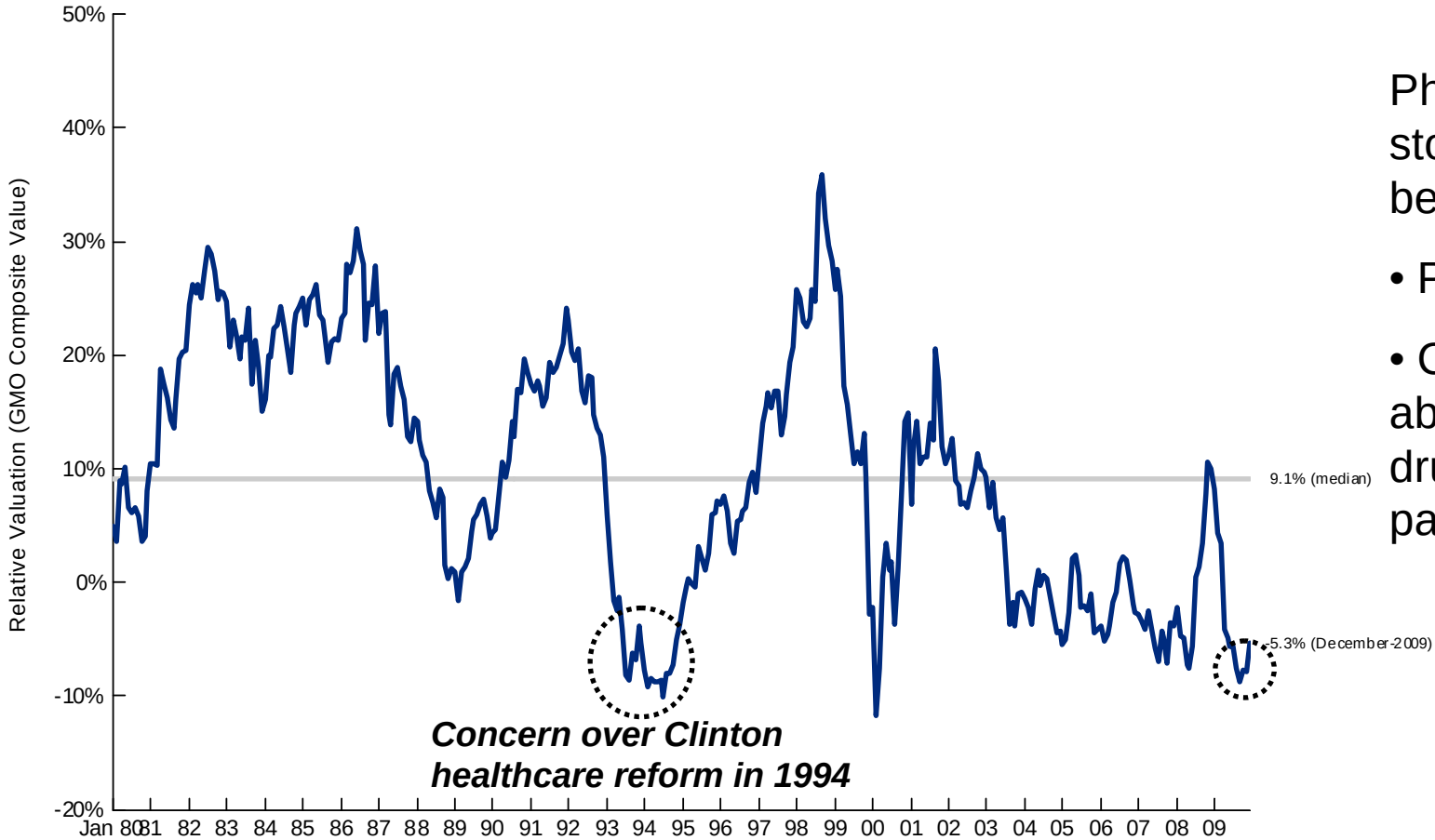


Chart shows the relative valuation of the cheapest 10% of the global markets as measured by GMO composite value.
Source: GMO Data as at December 2009

- The "valuation of value" fluctuates over time
- We have previously noted that the valuation of value gives some guidance on prospective returns
- Current cheapest "traditional" value opportunities trade in line with their historic averages
- From these levels they have typically outperformed by more than 5% p.a. for the next 3 years

The Valuation Of Pharmaceutical Companies

Pharmaceutical companies trade close to multi-decade low ratings



Pharmaceutical stocks have recently been held back by:

- Politics
- Concern over ability to replace drugs that are losing patent protection

Typical 3-year relative return from these levels: 10%+ p.a.

Source: GMO
Data as at end Dec 2009

Current “Tempering” By Momentum

Momentum ensures that sentiment is taken into account

Use of momentum ensures that the strategy is not aggressively underweight in these areas underpinned by strong sentiment:

1. ***Technology***

   Supported by restocking of inventory after the credit crunch

2. ***Materials***

   Supported by demand from China / India

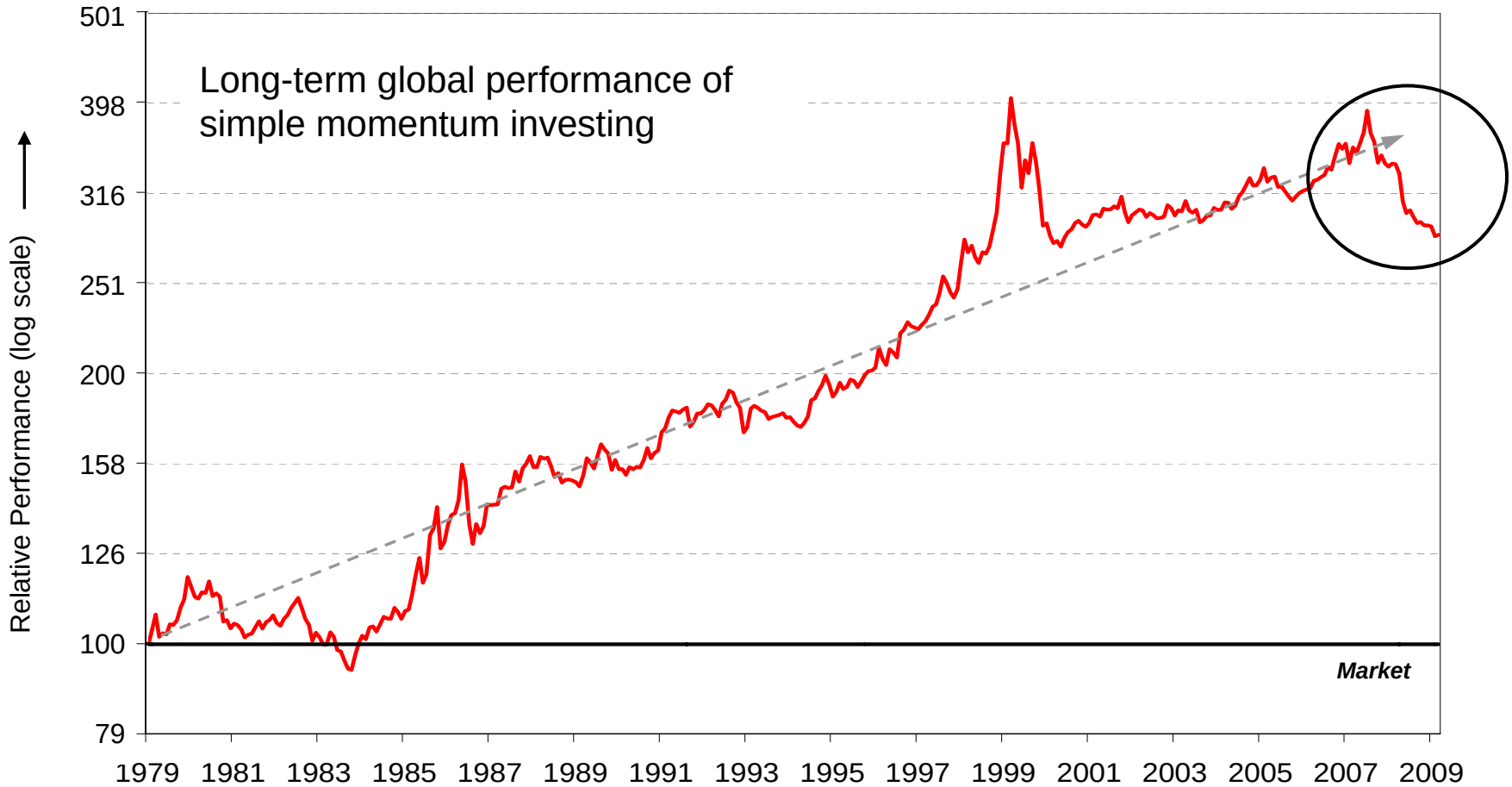
The momentum allocation is currently reducing portfolio risk relative to the benchmark

Summary

- Your portfolios lagged the market rebound that began in March 2009.
- The UK Core strategy struggles most during low quality markets and big turnarounds. 2009/10 has witnessed these two events at unprecedented levels and at the same time.
- The World Ex-UK strategy also had a bias towards higher quality and struggles when there are big market turnarounds.
- We are concerned that the global economy is not out of the woods yet and allied to this, equity markets do not look cheap.
- We believe that our stock selection techniques are well placed especially if markets behave as we anticipate.

Current Research Priority: Momentum

Is Momentum Losing Its Edge?

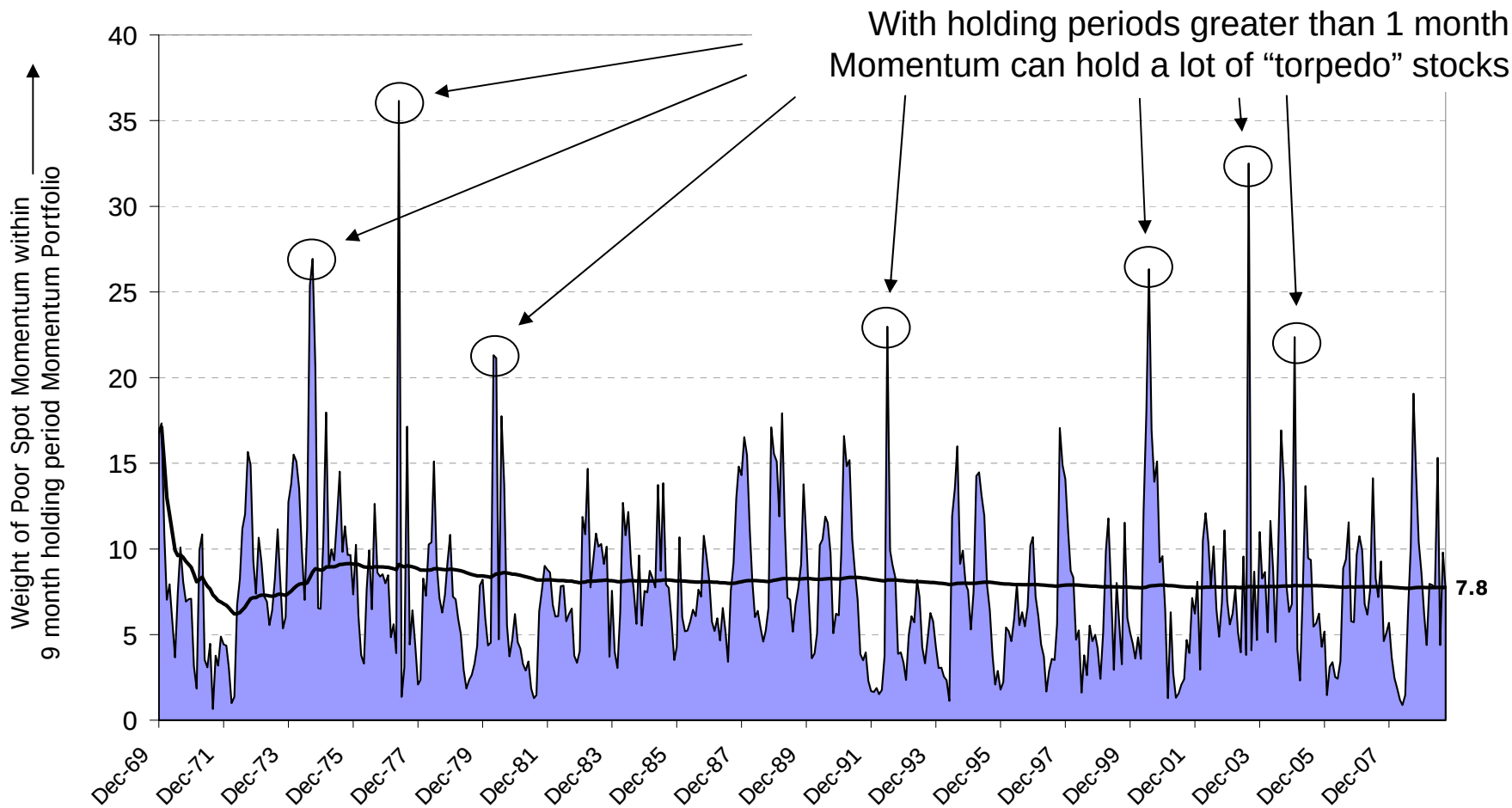


*Momentum is defined here as best 15% (by market cap) trailing six month price return using market cap weighting holding for 9 months

Source: GMO
Data as at 28 Feb 2010

Momentum Insight #1

Our methodology can hold on too long when Momentum changes

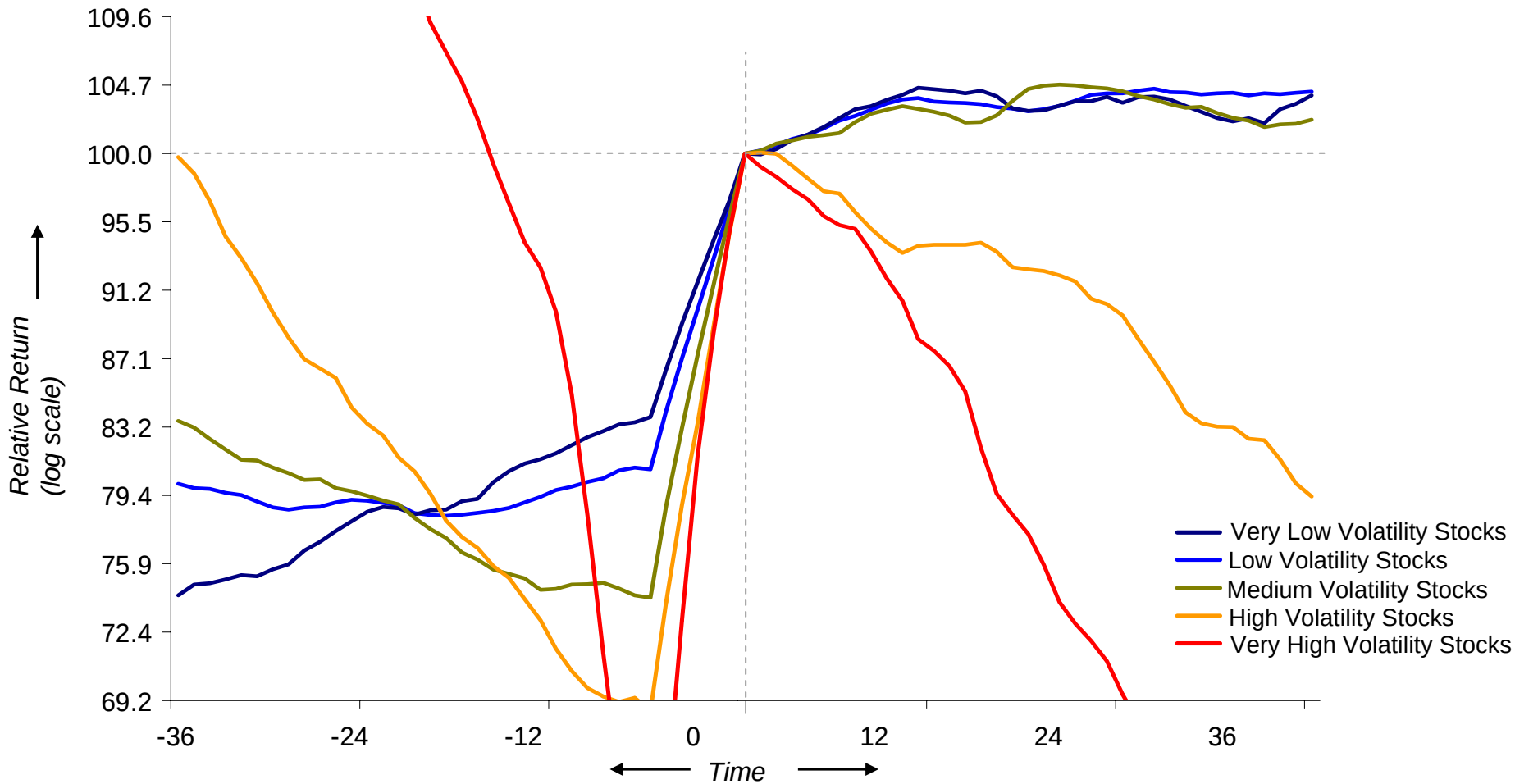


Overlap between worst 15% current Momentum and best 15% Momentum with 6m formation & 9m holding periods

Source: GMO
Data as at 30 Sept 2009

Momentum Insight #2

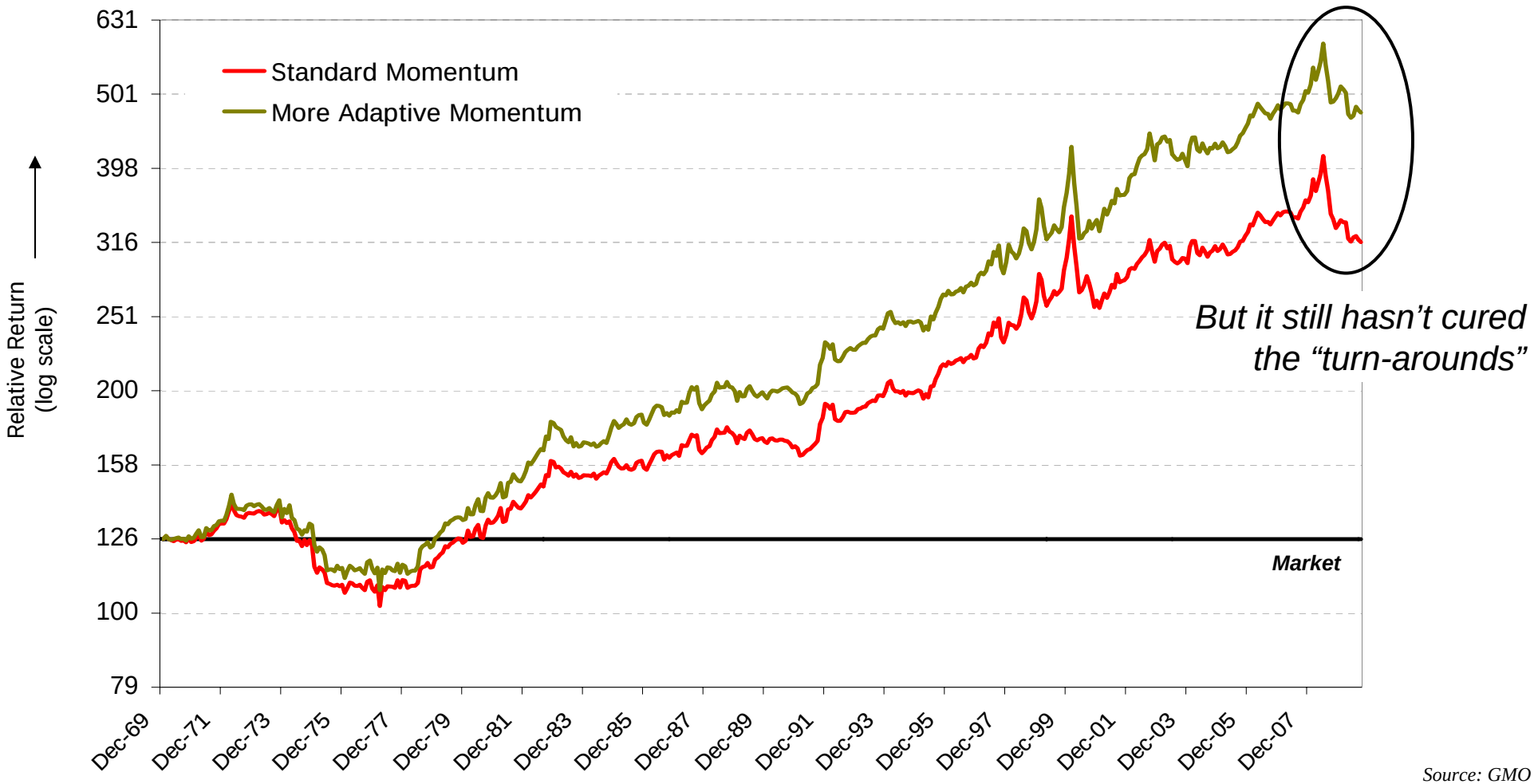
More Volatile Stocks Behave Differently



Analysis is performed on UK equities, 1986-2010; individual stocks are market cap weighted

Source: GMO

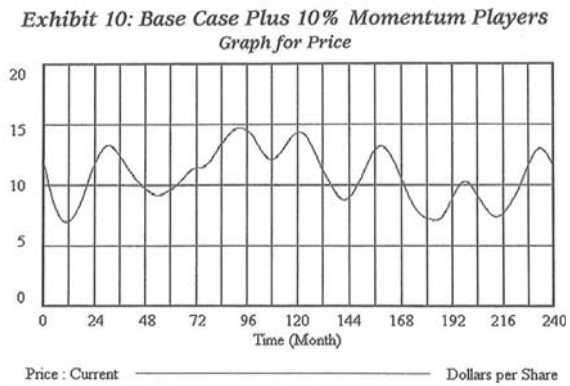
There Does Seem To Be Some Room For Improvement



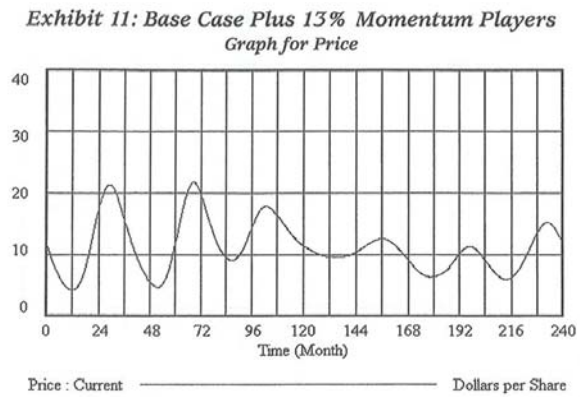
Standard momentum uses best 15% with 6 month formation & 9 month holding periods

Source: GMO
Data as at 30 Sept 2009

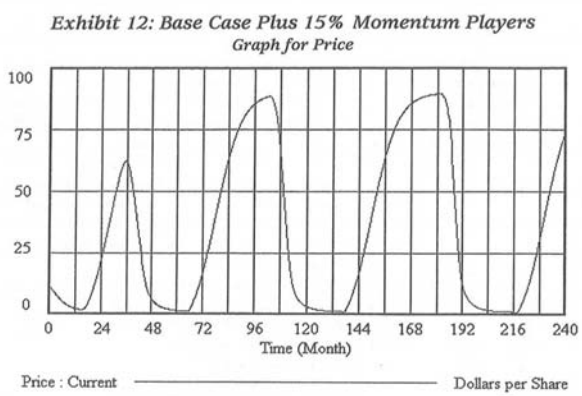
We Are Concerned That Turn-arounds May Be More Frequent Going Forward



Adding more momentum investors

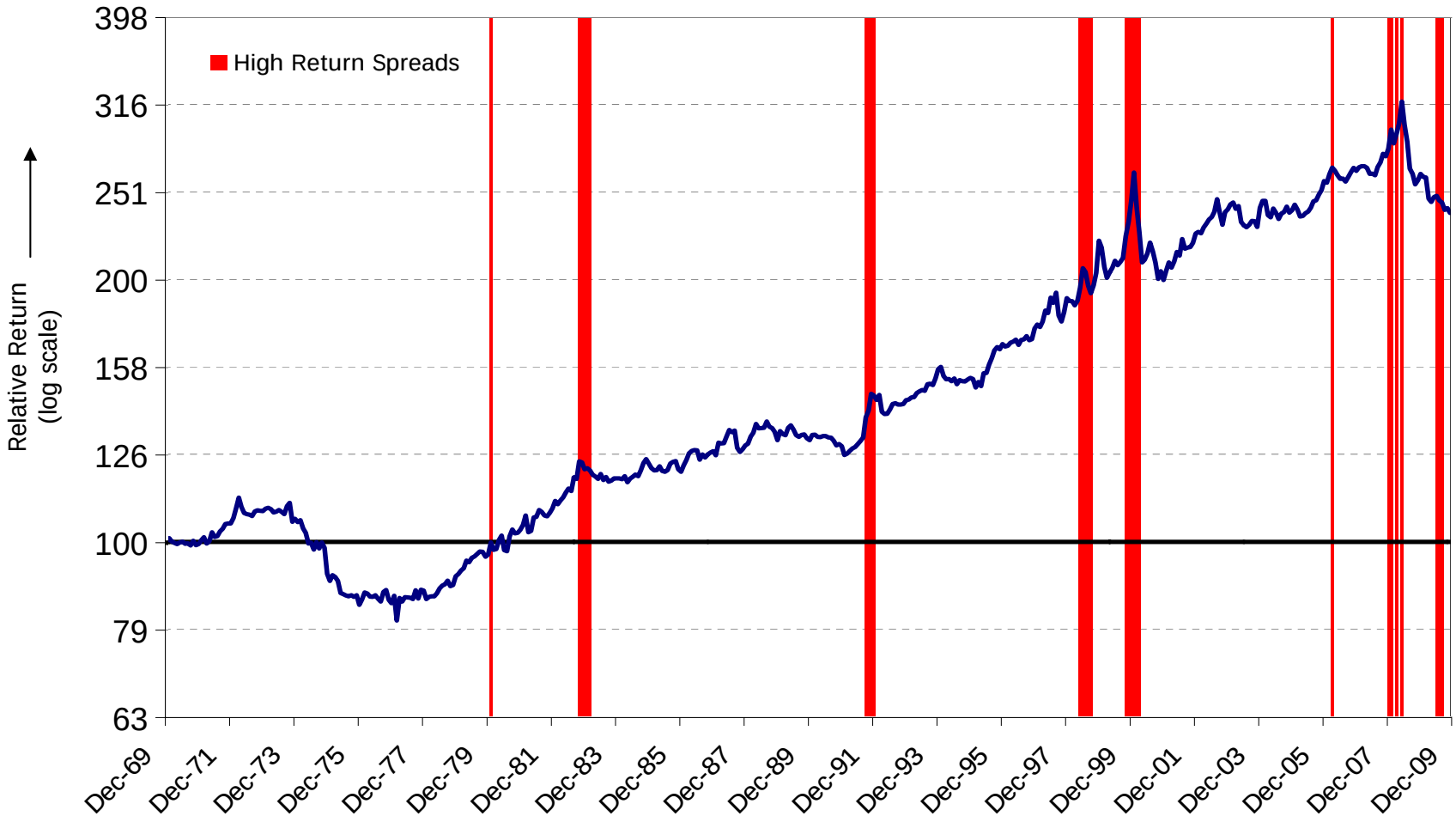


Adding more momentum investors



Source: Investing By The Numbers - Jarrod W Wilcox
Published by Frank J Fabozzi Associates, 1999
Copyright John Wiley & Sons

Are There Any Ways Of Anticipating Turn-arounds?



Momentum uses best 15% with
6 month formation & 9 month holding periods

Source: GMO
Data as at 31 Dec 2009

Appendix

GMO White Papers

China's Red Flags

Edward Chancellor - March 2010

Edward Chancellor, a member of GMO's Asset Allocation team, takes an in-depth look at today's China. He begins with a section on Identifying Speculative Manias and Financial Crises and follows with an analysis as to whether The China Dream is nearing an end given current signs of financial fragility.

Momentum - A Contrarian Case for Following the Herd

Tom Hancock - March 2010

Tom Hancock, co-head of GMO's Global Quantitative Equity Team, examines momentum investment strategies from the perspective of a long-only price momentum investor. Dr. Hancock also reviews current criticisms of momentum strategies and how they stack up against available data.

Deconstructing and Reconstructing Emerging Market Debt: A Bottom-Up Approach

Tina Vandersteel - March 2010

In this article, first published in the CFA Institute's Conference Proceedings Quarterly (March 2010), Tina Vandersteel discusses a methodology for determining whether investors in emerging market debt are being adequately compensated for all of the risks they are taking.

The Hidden Risks of Risk Parity Portfolios

Ben Inker - March 2010

Can risk parity portfolios deliver higher returns with lower risk when compared with a traditional balanced portfolio? In this white paper, Ben Inker, Director of Asset Allocation at GMO, discusses three problems he sees with risk parity portfolios.

Was It All Just A Bad Dream? Or, Ten Lessons Not Learnt

James Montier - February 2010

James Montier, a member of GMO's Asset Allocation Team, examines whether we learned anything from the market declines of 2008 and early 2009. In this paper, he outlines 10 of the lessons he believes not to have been learned.

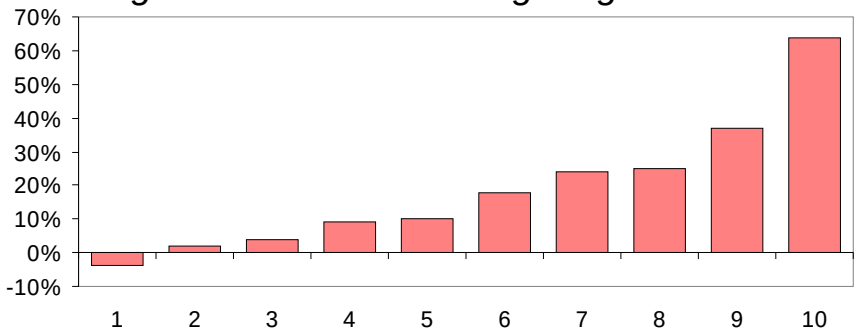
Stock Selection Techniques – Value

- Rank stocks at year end by PE and calculate fundamental and stock market returns*

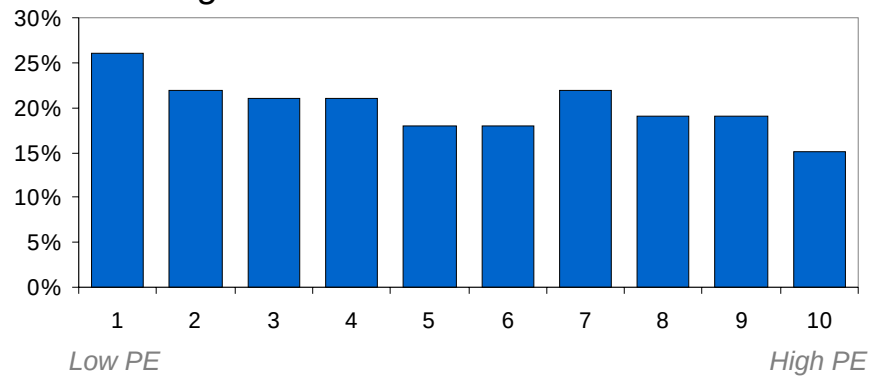
- Not surprisingly higher PE stocks have higher earnings growth

- But stock market returns are the inverse: higher PE stocks produce worse returns than lower PE stocks

Higher PE stocks have higher growth ...



But higher PE stocks have lower returns ...



**Analysis conducted on UK data from 1969 to 1997*

- *Markets and stocks are priced by market participants who are prone to common mistakes e.g. overpaying for excitement and underestimating mean reversion*
- *Value investing wins by purchasing out-of-favour stocks that are often uncomfortable to own*

Source: GMO; As at 30 June 2009

Quality Is A Crucial Ingredient When Valuing Stocks

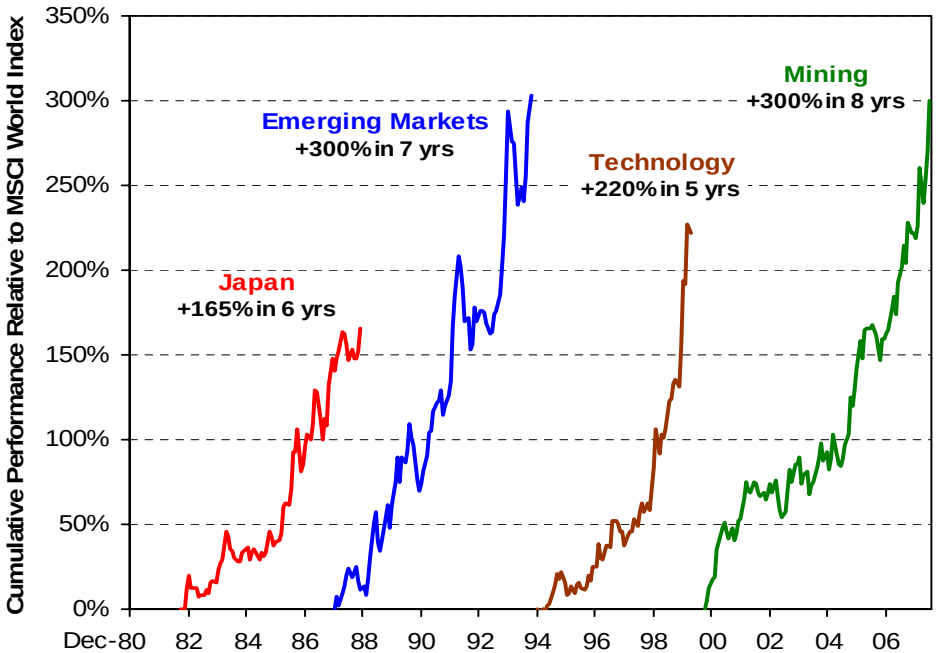
What do we mean by Quality?

High Quality	Low Quality
■ **High profitability**	■ Poor profitability
■ **Stable profitability**	■ Volatile profitability
■ **Low leverage**	■ High leverage
■ **Behaving like high quality**	■ Behaving like low quality
■ **High geographic spread**	■ Little or no geographic spread
■ **Low pension risk**	■ High pension risk
Reckitt Benckiser	*Royal Bank of Scotland*
AstraZeneca	*British Airways*
British American Tobacco	*Cookson Group*
GlaxoSmithKline	*Segro*
Imperial Tobacco	*ITV*
Vodafone	*Invensys*
Tesco	*Taylor Wimpey*
Unilever	*Mitchells & Butlers*

As at 31 Mar 2010
Source: GMO

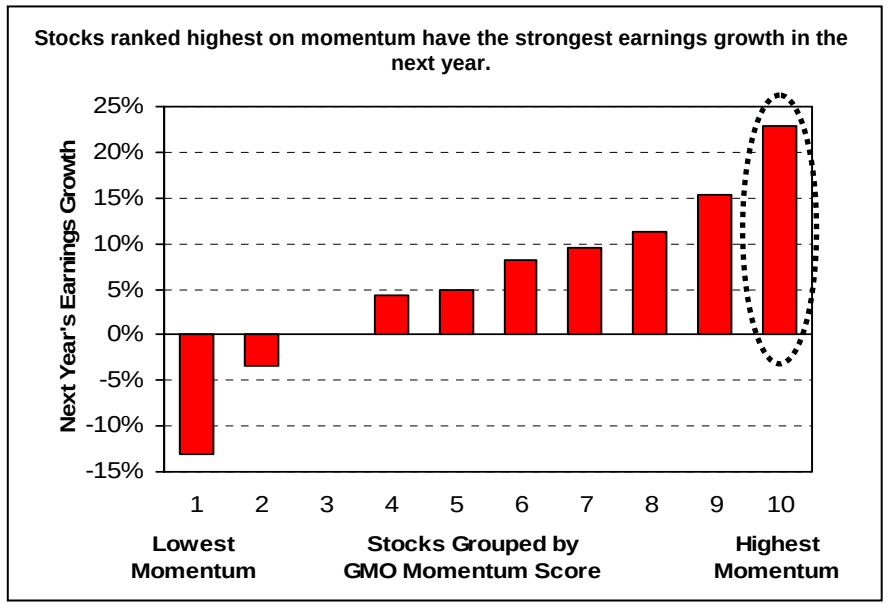
Stock Selection Techniques - Momentum

Momentum captures trends that may persist



Source: MSCI As of 30/06/08

Momentum predicts future earnings growth



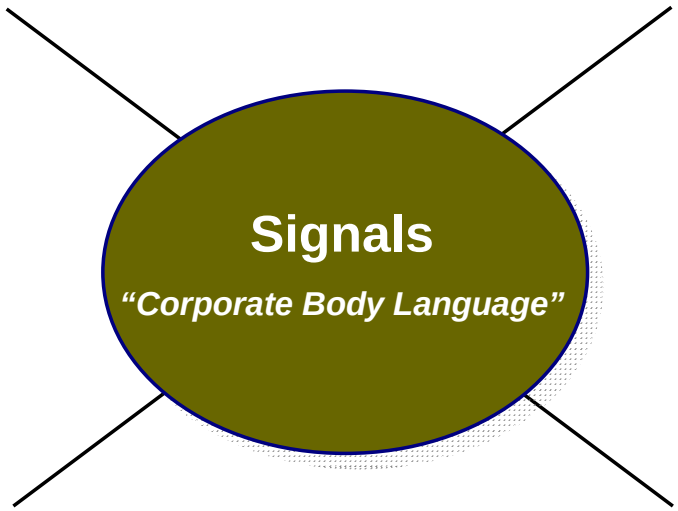
Note: *Based on aggregate back-tested data from 1980-2007*
Source: GMO As of 31/12/07

- *Momentum exploits the tendency for stocks and sectors to trend*
- *The simplest approaches are often the most effective*
- *Tends to perform extremely well during poor environments for Value investing*

Stock Selection Techniques - Signals

Market
Analyst estimates
Profit warnings

Management
Directors dealings
Business decisions
Corporate governance



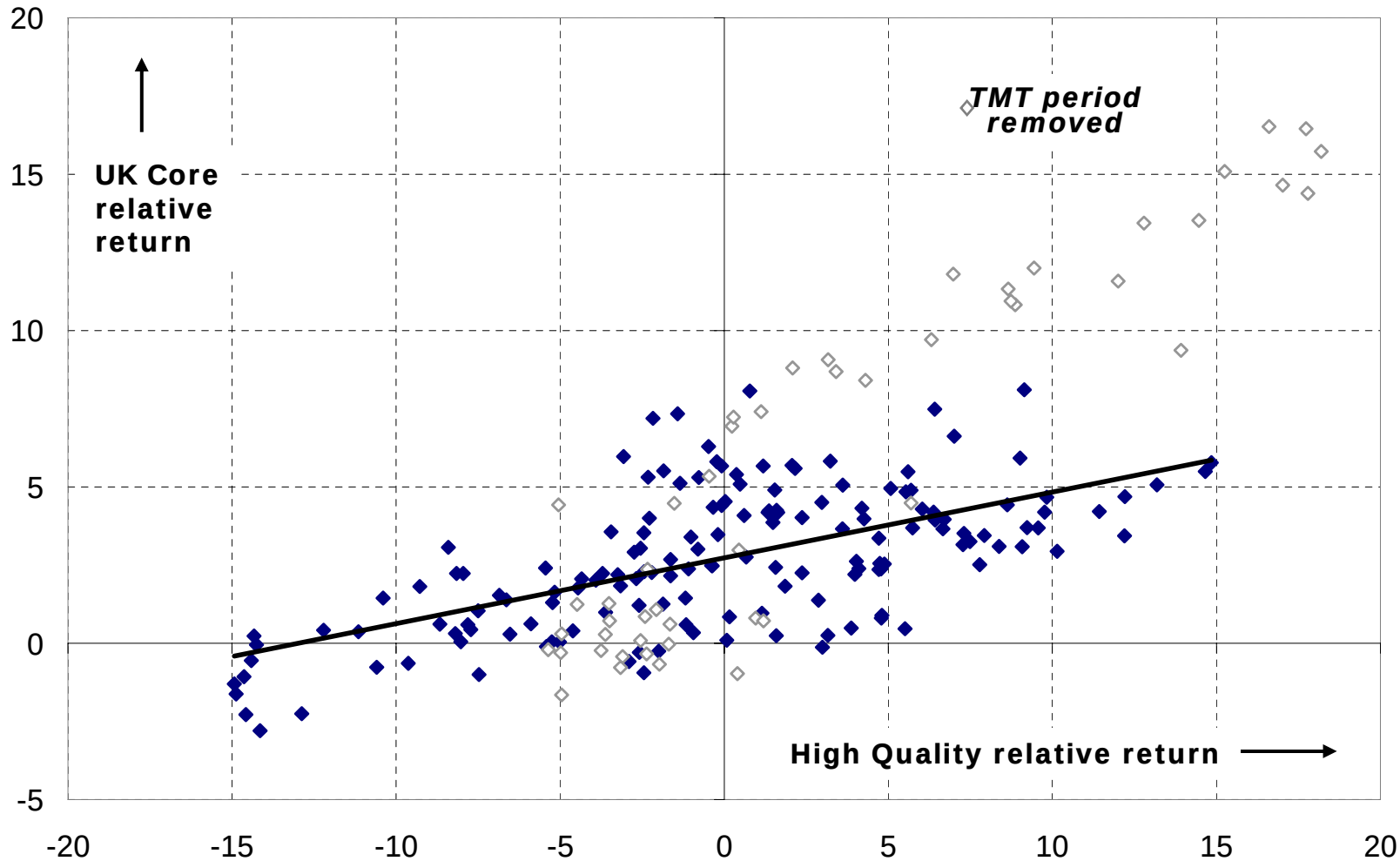
Overambition
Equity issuance
Takeovers
Excessive growth

Accounting
Aggressive accounting
Operational signs

- *Signals uses a broad array of inputs classified into four groups*
- *Inputs tend to be early warnings signs or indicators of good or bad business practice*
- *Typically captures information that takes time to be fully reflected by the market*

UK Core Strategy Struggles In A Low Quality Driven Market

What are the factors that have historically influenced returns?



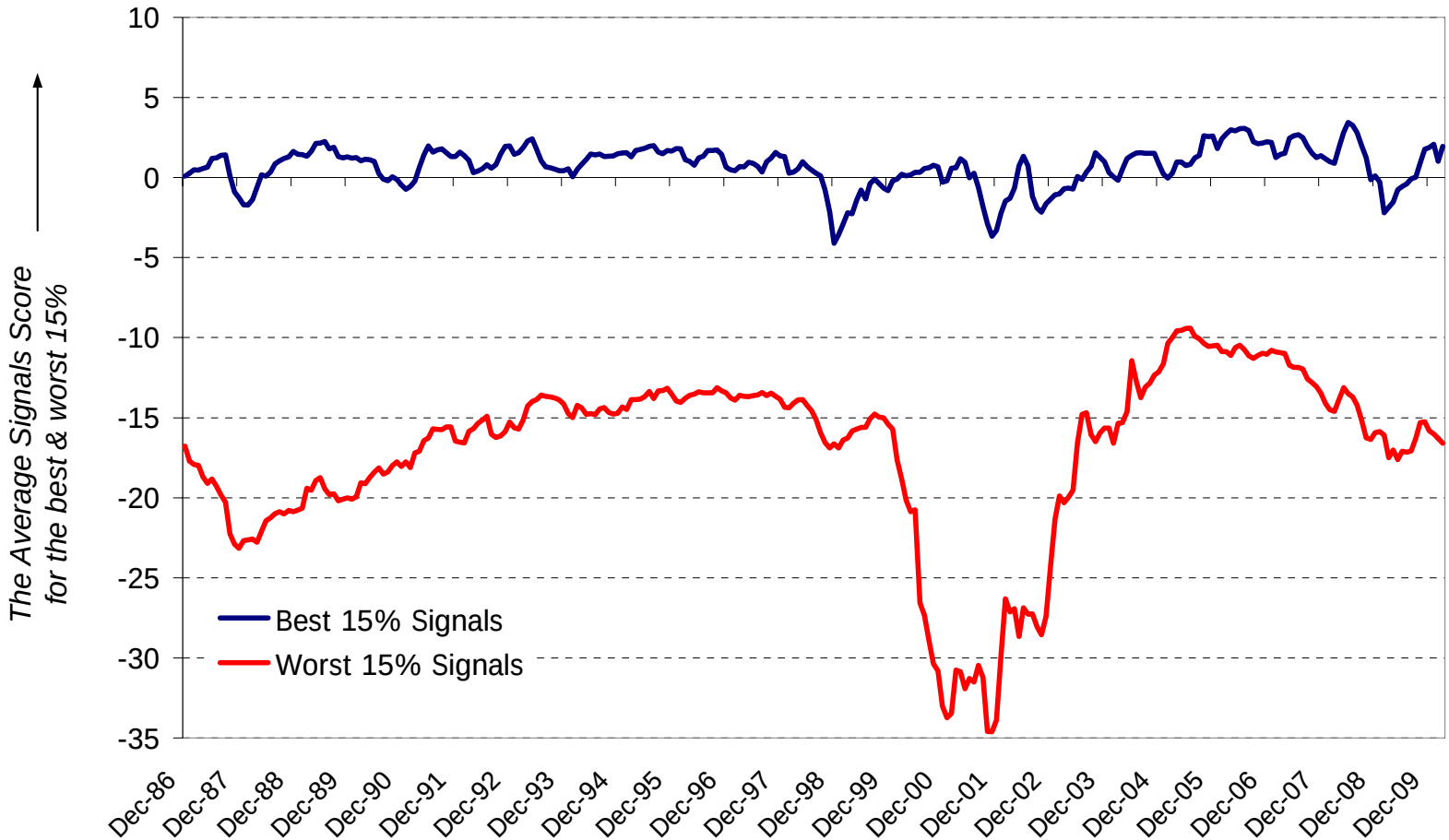
1986-2005

Source: GMO London Investor Conference 2005

GMO

The Spread Of Signals Has Been Widening

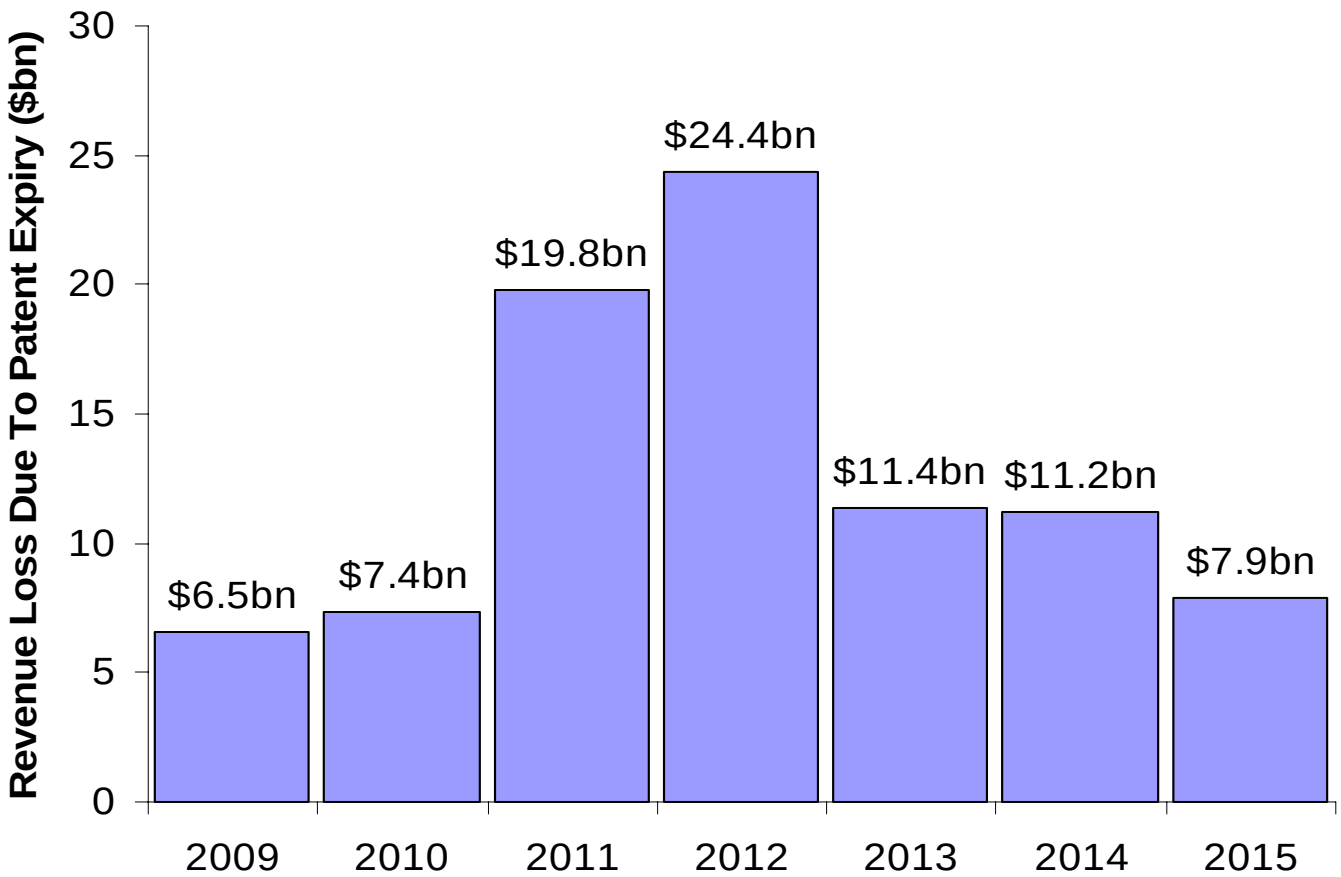
The greater the spread between good and bad signals, the greater the opportunities



Source: GMO
Data as at 31 Mar 2010

Revenues At Risk From Patent Expiry, 2009 - 2015

There is a "patent cliff" in 2011/12 and these revenues will not be replaced in full



- Pharma companies get patents on their drug developments
- The patents last for 20 years
- When the patent runs out, the company must replace the revenue from another development or else shrink
- In 2011/2012, many patents will expire, casting a shadow over near-term growth

Revenues of the US Pharma sector were $282bn in 2008

Source: Barclays Capital
Data as at end Dec 2009:

Estimating The "Worst Case" Scenario For Pharma

We made some draconian assumptions about the next few years for the Big 6 Pharmas

1) Focus on the Big 6

Johnson & Johnson Abbott Lilly

Bristol-Myers Squibb MERCK Pfizer

2) Identify significant patent expiries up to 2013

3) Assess stock prices under draconian assumptions:

- All revenue from patent expiries is lost immediately
- Only direct manufacturing costs can be cut
- $35bn annual R&D fails completely

Source: GMO
Data as at end Dec 2009

Estimating The "Worst Case" Scenario For Pharma

Pharma has a good chance of winning because the trouble is already in the price

	2010 Sales	Sales At Risk	"Worst Case" Profits	"Worst Case P/E"
Abbott	32,901	-5%	6,833	16.3
Bristol Myers Squibb	19,885	-51%	-979	n/a
Johnson & Johnson	63,825	-5%	14,742	16.1
Eli Lilly	22,863	-21%	2,448	22.3
Merck	45,213	-17%	7,710	19.3
Pfizer	67,243	-31%	9,175	21.3
Total	**$251,930**	**-19%**	**$39,929**	**20.4**

The Big 6 have a fifth of their business at risk between now and 2013

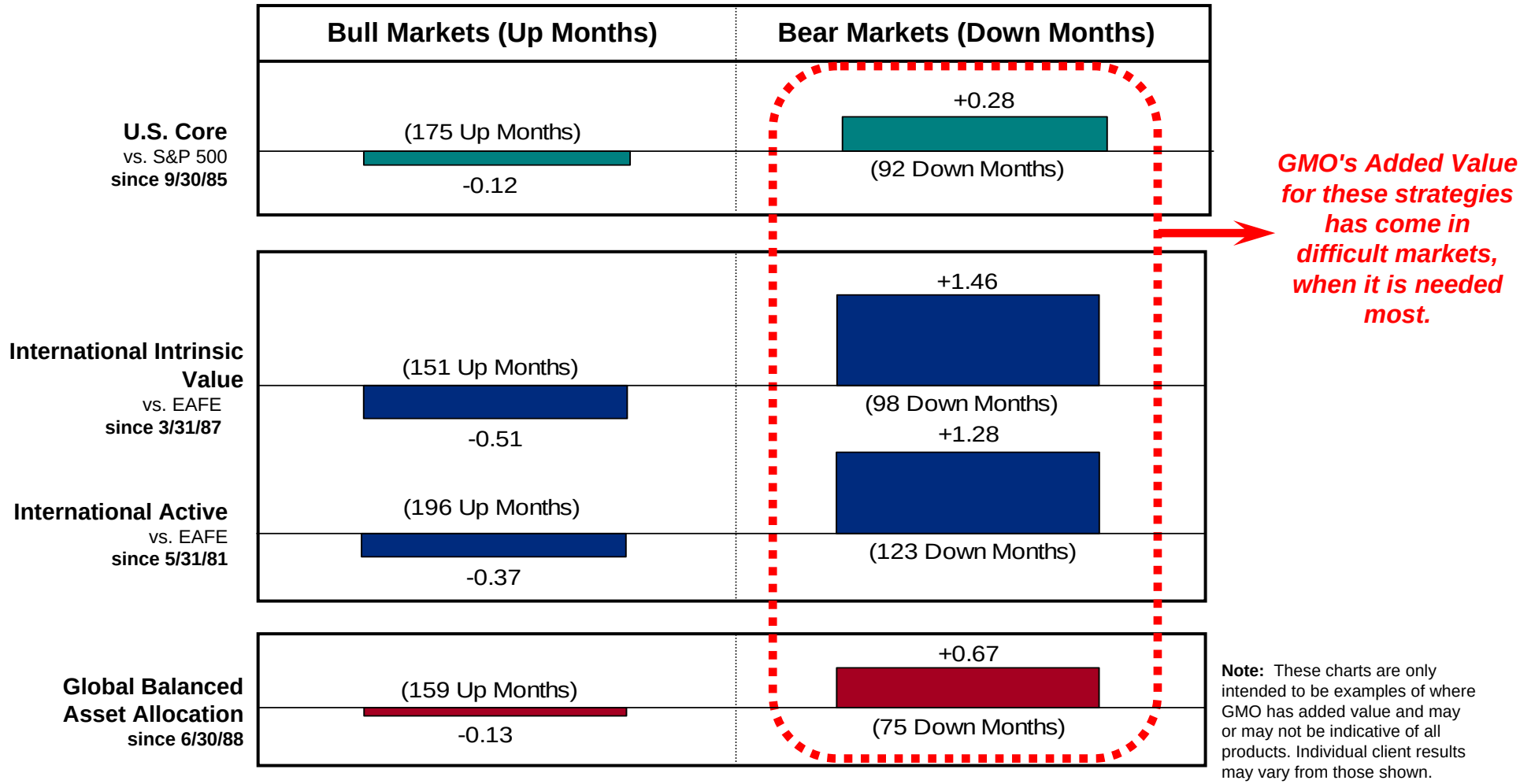
Even under our harsh assumptions five of the six would make profits

And they would still trade close to the market's normalised P/E of 19.2

Conclusion: Pharmaceutical companies are priced to withstand a worst case outcome, and there is scope for a pleasant surprise

Source: DrugAnalyst,GMO
Data as at end Dec 2009

GMO's Approach Has Historically Excelled In Difficult Market Environments



Note: These charts are only intended to be examples of where GMO has added value and may or may not be indicative of all products. Individual client results may vary from those shown.

Performance data quoted represents past performance and is not predictive of future performance. Returns are shown after the deduction of management fees, transaction costs, and other expenses. The returns assume the reinvestment of dividends and other income. A GIPS® compliant presentation of composite performance has preceded this presentation in the past 12 months or accompanies this presentation, and is also available at www.gmo.com. Actual fees are disclosed in Part II of GMO's Form ADV and are also available in each strategy's compliant presentation.

GMO Overview

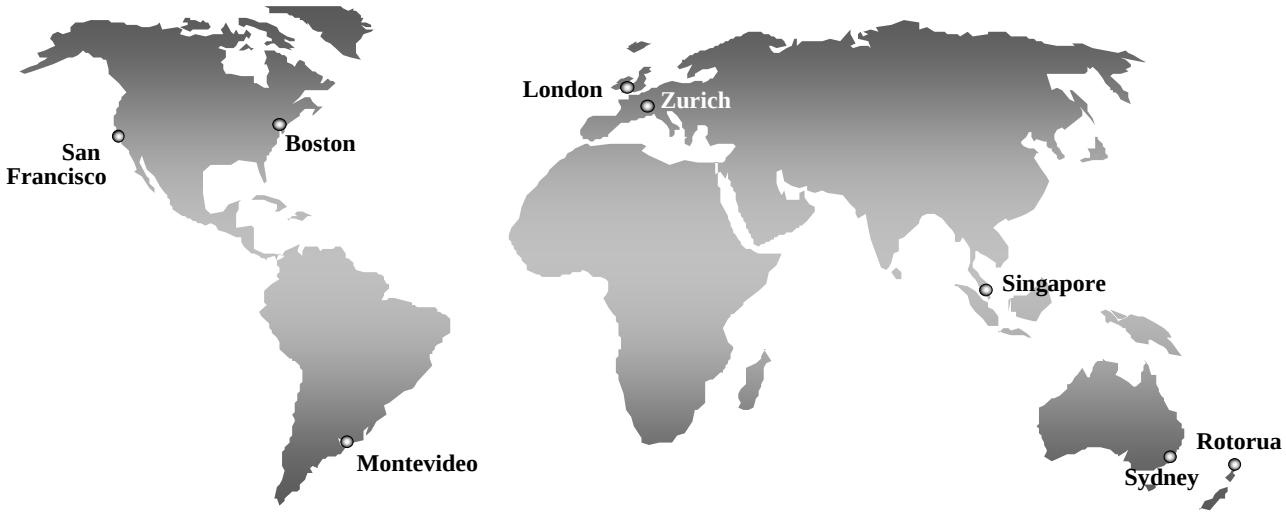
- Global firm - private partnership, investment management is sole business
- Institutionally focussed business that has been in the UK since 1987 with a long-serving investment team
- Quantitative approach that offers rigorous and emotion free decision making

Assets in excess of £70 billion

- £62 billion in equities
- £8 billion in fixed income
- £23 billion in asset allocation*
- £6 billion in absolute return strategies*

People

- More than 100 investment professionals
- More than 500 employees worldwide
- 43 active partners



* Asset allocation and absolute return assets are accounted for within underlying strategies and should not be double-counted.
Represents assets from both GIPS and non-GIPS compliant firms. There are two GIPS compliant firms. The first is Grantham, Mayo, Van Otterloo & Co. LLC ("GMO"), an independent investment adviser registered under Investment Advisers Act of 1940. GMO's accounts are managed by investment management offices in Boston, MA and Berkeley, CA. GMO has total assets of $97,247,951,138 (USD). The second firm is defined as GMO UK Limited. GMO UK was established to manage mandates primarily for UK and other European clients. GMO UK is authorized and regulated by the Financial Services Authority in the United Kingdom. GMO UK firm assets are $3,368,302,123 (USD).

As of 31/3/10 (prelim.)

Performance data quoted represents past performance and is not predictive of future performance. The foregoing does not constitute an offer of any securities for sale. Returns are presented gross of management fees, net of transaction costs and include the reinvestment of dividends and other income. If these expenses were deducted performance would be lower. For example, if the strategy were to achieve a 10% annual rate of return each year for ten years and an annual advisory fee of 0.75% were charged during that period, the resulting average annual net return (after the deduction of advisory fees) would be 9.25%. A GIPS compliant presentation of composite performance has preceded this report in the past 12 months or accompanies this presentation, or is also available at www.gmo.com. Actual fees are disclosed in the Prospectus for each fund and are also available in each strategies compliant presentation.

Performance is shown compared to broad-based securities market indices. Broad-based indices are unmanaged and are not subject to fees and expenses typically associated with managed accounts or investment funds. Investments cannot be made directly into an index.

GMO

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