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Investments of the United Nations Joint Staff Pension Fund and measures undertaken to increase diversification

Report of the Secretary-General

I. Introduction

1. The management of the investments of the assets of the United Nations Joint Staff Pension Fund is the fiduciary responsibility of the Secretary-General of the United Nations, who acts in consultation with the Investments Committee, taking into account the observations on broad policy of the United Nations Joint Staff Pension Board and the General Assembly. The Investments Committee provides advice to the Secretary-General on investment strategy and reviews the investments of the Fund at its quarterly meetings. The Assistant Secretary-General for Central Support Services has been designated as the representative of the Secretary-General for the investments of the Fund, and has been delegated the responsibility for the oversight of the investment of the assets of the Fund on behalf of the Secretary-General. The representative is assisted by the staff of the Investment Management Division. All investments must, at the time of initial review, meet the criteria of safety, profitability, liquidity and convertibility.

2. The present report provides information on the management of the investments of the Fund during the period from 1 April 2008 to 31 March 2010 and on investment returns, diversification of investments and development-related investments of the Fund.

II. Changes during the biennium

3. During the biennium ended 31 March 2010, the financial markets were rocked by shock waves from the deepest and most synchronized economic contraction since the Great Depression. The bankruptcy in September 2008 of Lehman Brothers was the largest financial bankruptcy in history, making lenders worldwide fearful about trusting any counterparties. The effect on borrowing conditions was profound, hampering the abilities of countries and companies to obtain funding. Assistance

from the International Monetary Fund (IMF) was required by a record number of countries, while individual central banks intervened in a variety of ways to support crippled financial institutions. The emergency responses of Governments themselves created concern about unfair support mechanisms, with Government-guaranteed deposits, for example, attracting funds from other parts of the banking system.

4. The recovery in global equities that emerged out of the March 2009 cycle low point can be summed up as a synchronized sigh of relief. Markets regained their bearings from the deepest and most synchronized economic contraction since the Great Depression, and risk appetites improved, as evidenced by the outperformance of the weakest elements of the banking sector, some real estate companies, low-quality equities and even junk bonds. The Investment Management Division underweighted equities substantially during the financial crisis and increased equity holdings after the recommendation of the Investments Committee in February 2009 and until March 2010 by purchasing over $2 billion worth of equities. Helped by the rise in market value, the equity weighting of the portfolio was raised from 51.9 per cent as at 31 March 2009 to 65.6 per cent as at 31 March 2010.

5. The fiscal year-end balances of the Fund for 2008, 2009 and 2010 of $40.6 billion, $29.0 billion and $38.3 billion, respectively, reflect the benefits of prudent stock selection, global diversification and tactical rebalancing. The Investment Management Division has captured the benefits of the positive market trends and has also worked to strengthen the investment infrastructure and reduce the costs of transactions.

6. For the two-year period ending 31 December 2009, the Fund realized a net gain of $412 million. Amid the unprecedented volatile markets, the Fund had unrealized gains of $6,223 million as at the end of 2009 and realized gains of $3,152 million. The Fund also incurred realized losses of $2,741 million in gross terms through trading activities aimed at improving the overall quality of the portfolio. The realized losses were mainly generated in conjunction with the disposal of poorly performing instruments.

7. Over the longer term, the Fund outperformed the 60/31 benchmark over the last 3, 5, 7 and 10 years. In the long run, through active management, the Fund will endeavour to outperform the policy benchmark with effective stock selection and periodic rebalancing of assets to maintain the Fund’s long-term investment objectives. The Investment Management Division continues to focus on balancing risk and reward expectations by apportioning the Fund’s assets according to allocation goals that are appropriate for a long-term investment horizon.

8. The salient feature of the recovery in the global equities markets is how very uneven it has been. The developed countries, with greater access to global bond markets, relied more on debt than was healthy. While leverage can increase the return on capital when times are good, the burden of debt becomes a constraint during recessionary times. The process of deleveraging in the developed markets will continue for a few more years, and small companies may have less access to financing, putting a damper on company performance and economic growth. Fortunately, since 2007 the Investment Management Division has emphasized investments in markets in which leverage and governance are the most protective. Countries and companies with sound balance sheets recovered more quickly. The tracking of leverage and credit risk, initiated in 2007, has contributed to the Fund’s outperformance.

9. During this volatile period in the equities markets, the emphasis of the Investment Management Division has been to build the infrastructure of the Fund to safeguard the principal and to support better investment decisions. Regardless of market direction, there are some costs which can be controlled, such as brokerage, custody and advisory services. Moreover, the use of risk management and analytical tools in the decision-making process can improve the long-term performance of the Fund. To achieve these objectives, a record number of competitive procurement exercises have been launched: to procure and implement the trade order management system, risk management software, brokerage services, trade execution analysis, investment advisory services, portfolio accounting, custody and independent master record-keeping services.

10. In January 2010, the Investment Management Division inaugurated the use of an electronic trade order management system and integrated it with the secure Society for Worldwide Interbank Financial Telecommunication (SWIFT) financial telecommunications system, which went live at the time of the last Pension Board meeting. These systemic improvements create an infrastructure that will benefit the Fund for years to come, reducing costs and enhancing the security of funds transfers.

11. With improved infrastructure, the Fund is now a safer client, meeting the highest industry standards. Counterparties do not have to worry that an order sitting in the in tray of the fax machine might be stale, a duplicate or a fraud, because the system incorporates the required dual controls. No single person can launch a transaction, preventing the risk of “rogue trades”. Pre-trade compliance features have been incorporated into the trade order management system, ensuring that investment orders are not transmitted to brokers until they are checked for conformity with investment policies.

12. The Investment Management Division has successfully implemented a trade order management system to replace the current fax-based order placement procedure and to enhance the security and execution capability that will lead to the best execution. Since the first trade on 8 January 2010, security transactions for equity, fixed income, foreign exchange and cash have been gradually shifted to the new system. Between 30 May 2010 and 31 August 2010, trades with a value of over $3.74 billion were executed through Charles River.

13. The automated trade order management system means that not only are the orders placed more securely, but also that the system reports back at every step of each transaction, allowing for a better audit trail. The transparency of an audit trail has other benefits than confirming that a transaction was duly authorized and by whom. The Investment Management Division can now tell when the brokerage firm received the order to purchase a stock, and can determine if the broker executed the transaction at a fair price. With access to trade execution data, the Division is now able to quantify the execution quality and to grade brokerage services based on accurate market pricing data. It is estimated that better execution could improve the returns of the Fund by $100 million to $200 million per year. It is the intention of the Division to conduct a trade execution analysis of brokerage services on an annual basis to ensure that transaction prices are appropriate.

14. Aware of the reputational hazards of operating in the financial services industry, the Investment Management Division has not only met the requirements of the United Nations financial disclosure programme, but has also inaugurated policies regarding personal securities and gifts and hospitality, in order to affirm the

Division's commitment to the highest standards of ethics, good governance and integrity. The basis for the personal securities policy is that the United Nations financial disclosure programme is a single-point-in-time assessment that does not provide the continuous oversight needed to monitor the personal trading activities of Investment Management Division personnel compared with the investment actions of the Fund. The revised policy has been adopted in accordance with international best practices for the prevention of fraudulent or manipulative practices with respect to purchases or sales of securities held or to be acquired by the Fund.

15. It has been the consensus of member organizations for some time that the Fund should retain its strong internally managed structure, outsourcing investments only for narrow mandates such as small capitalization companies, real estate or private equity for which the Investment Management Division cannot employ the requisite specialized talent in staff positions. At the same time, it has been noted that, in order to identify the appropriate investment opportunities, discriminate among the plethora of equity offerings and manage risks safely, Division staff need the same tools as are used by their competitors in other investment organizations.

16. One of the most important tools of the trade that was lacking in the Investment Management Division was modern risk management. For this reason, the Investment Management Division, with the assistance of the Procurement Division, launched a request for proposal for risk management software. Following extensive due diligence, the Investment Management Division selected RiskMetrics as the risk analytics and performance measurement tool for the Fund. RiskMetrics is the leading supplier of portfolio risk analytic, performance and portfolio optimization software, supporting all the asset classes and currencies into which the Investment Management Division diversifies the investments of the Fund. The performance attribution module will produce portfolio performance attribution, including an analysis of the currency contribution, and will decompose total performance into the various components of return. The portfolio optimization module will enable investment officers to optimize the portfolio in order to obtain the best risk-adjusted returns. In addition, RiskMetrics can stress test the portfolio for various potential economic shocks (e.g., widening credit spreads, rising interest rates, oil price shocks and terrorist attacks). The representative of the Secretary-General and the Director of the Investment Management Division signed the contract with RiskMetrics in May 2010.

17. The Investment Management Division has used the current non-discretionary adviser model since the inception of the Fund. The current advisory framework is outdated, as has been documented in outside studies conducted by Mercer, Deloitte and Trocollo. Because the business of offering non-discretionary advice is waning to the point that it has become a rarity, there is an inherent scope for conflicts of interest. The Investment Management Division recommended a new framework that would break down the current wide range of advisory services into new, more specific categories and eliminate the existing redundancies. The enhanced framework, which was reviewed by the Investments Committee in July 2009, will incorporate focus advisory services into three categories: strategy advisers, research providers and investment platforms. The Procurement Division is in the process of conducting competitive bidding for strategy advisers, research providers for equity and global macro/sector, and equity analytical software.

18. To further enhance the proposal of the Investment Management Division, the Investments Committee suggested the introduction of leadership funds to obtain real-time and real-money advice about strategic and tactical asset allocation from the top talents in the industry. The organizations of the candidates for leadership funds should possess longevity, excellence and independence in management; strong investment team structure and decision-making processes; and a superior client base that includes pension funds and sovereign wealth funds. Based on discretionary advisory services, the Division will establish more effective and timely advice from advisers while avoiding potential conflicts of interest. The Division will review the practical implementation after the establishment of broader resources, including the alternative assets adviser, for which the Procurement Division is also in the process of competitive bidding.

19. To strengthen the investment management process, the Investment Management Division has implemented an ongoing system for documenting the logic behind each investment purchase and key risk factors to monitor. For each investment held in the portfolio, the investment rationale will periodically be re-examined to ensure that profits are taken when appropriate, or that sell discipline is imposed when necessary. The investment rationale document will be electronically linked with each investment in the Charles River trade order management system.

20. The Investment Management Division is continually seeking opportunities to diversify the portfolio further in order to enhance the risk-return profile of the Fund. The Division has selected a senior investment officer for alternative investments, and has signed a contract with a private real asset adviser to provide guidance regarding infrastructure funds and agricultural and timber lands. The Division also signed a contract with the African, Latin American and Caribbean Fund, which is managed by the International Finance Corporation Asset Management Company, on 30 June 2010. The Investments Committee concurred with that approach at the meeting held on 10 May 2010. A request for proposal for a non-discretionary adviser for private equity and hedge funds of funds was issued, and the technical evaluation is being finalized.

21. In December 2008, a new five-year contract was awarded to Nikko Asset Management as the Fund’s non-discretionary adviser for global asset allocation and Asian equities following competitive bidding. The contracts of non-discretionary advisers Fiduciary Trust Company International and BNP Paribas were extended until 31 December 2010. These advisers are responsible for the major areas of the Fund’s investments, including global asset allocation, the global fixed income portfolio and equity portfolios for North America, developed and emerging Europe, Latin America, the Middle East and Africa. The Investment Management Division prioritized the selection process for a fixed income adviser owing to the scarcity of internal resources and the significance to the Fund. The Investment Management Division, with the assistance of the Procurement Division and the Office of Legal Affairs, is currently working on the contract with the vendor.

22. A new contract was awarded to the Fund’s United States of America small capitalization account manager Fisher Investments on 1 December 2009 and to Eagle Asset Management on 4 January 2010. The Investment Management Division has increased the allocation to this asset category, as agreed by the representative of the Secretary-General following the 19 October 2009 Investments Committee meeting. As at 31 March 2010, the United States portfolio had $741 million invested with two

external managers, representing approximately 7 per cent of the total United States portfolio, compared with 4.6 per cent ($442 million) as at 31 August 2009. This compares with the Investments Committee recommendation of 8 per cent plus or minus 2 percentage points. In addition to previously held equity assets, the Investment Management Division increased the investment with these managers by $55 million (Eagle) and $95 million (Fisher) coincident with the respective transitions. Subsequently, a further $75 million was placed with Fisher at the end of March. As such, the current allocation between these managers is approximately 35 per cent Eagle (small capitalization “core” style) and 65 per cent Fisher (small capitalization “value” style). Going forward, it would be desirable for the Investment Management Division to secure a small capitalization growth manager in order to achieve a balance of styles among the small capitalization assets; it would be desirable to add a growth-oriented manager to the portfolio. The Investment Management Division will continue working with the Procurement Division and engage the services of an independent consultant to streamline the process for hiring specialized fund managers, in keeping with industry best practices.

23. A new five-year contract was also awarded to the Fund’s European small capitalization account manager Baillie Gifford on 17 October 2008. The approval to award a second European small capitalization account contract to Dimensional Europe was received. Owing to the market environment, the Fund has decided not to increase its allocation in European small capitalization companies and has not proceeded with awarding the contract to Dimensional Europe. Similarly, the contract with a new manager for Japanese small capitalization accounts was signed with an effective date of 1 August 2010.

24. The Investment Management Division, with the assistance of the Procurement Division, is currently conducting the Fund’s first-ever request for proposal for equity brokerage services. This request for proposal was initiated to address longstanding recommendations to document the Investment Management Division’s relationship with brokers in formal legal agreements so as to satisfy the requirements of the Financial Rules and Regulations of the United Nations. The request for proposal for equity brokerage services also represents an opportunity for the Investment Management Division to review and improve its broker selection and evaluation process, and will result in more effective procedures as well as enhanced fairness and transparency. As a result of the financial evaluation to be conducted by the Procurement Division, the Investment Management Division will benefit from a more competitive fee schedule and a reduction of its trade execution costs.

25. The indexation of the North American equities portfolio, endorsed by the Board in July 2006, and the administrative cost for implementation approved by the General Assembly in December 2006 have been deferred owing to the credit crisis that started in August 2007. The focus of the Investment Management Division has been on the preservation of capital. So long as the ongoing financial crisis continues, avoidance of the most vulnerable market sectors is especially critical. This has been achieved, so far, by active management.

26. Indexation is a tool that can be used to provide flexibility in managing the assets of the Fund, in particular for the fine tuning of asset allocation. Because indexation approximates the returns of financial markets as a whole, it is a tool that can be most advantageously used in rising markets. In this regard, the Investment Management Division conducted a review of potential rebalancing tools in January

2009, which was presented to the Investments Committee at the 9 February 2009 meeting. Various index funds, equity index futures and basket approaches were considered as possible tools for quickly and efficiently raising the proportion of common stocks held in the portfolio. The Division is of the opinion that the standard index funds may not be in compliance with the Fund's policies prohibiting investments in tobacco and defence. While equity index futures are cost-effective and efficient, the necessary infrastructure, including SWIFT and a trade order management system, are prerequisites. During the implementation of the necessary secure infrastructure, the Division recommended the use of the basket approach for increasing the equity weighting. In 2008, the Investments Committee concurred with that recommendation, but urged the Division to implement the necessary information technology infrastructure. In 2010, having completed the infrastructure enhancements, the Division will implement the rebalancing tools for a more streamlined way of adjusting the tactical asset allocation of the Fund.

III. Economic review

27. On 20 September 2010, the National Bureau of Economic Research "officially" declared that the United States recessionary period was over, and the above data points clearly indicate that a recovery has taken hold. Given the fourth quarter 2007 start of the slowdown, per the National Bureau of Economic Research, this "Great Recession" was among the longest-duration recessionary periods on record. That said, United States corporate profits, as measured by Bureau of Economic Analysis data, actually bottomed out in the fourth quarter of 2008 (declining 25 per cent year-over-year on an annualized basis). By the fourth quarter of 2009, one year later, profits had rebounded at a near record 31 per cent rate. This rapid recovery can be attributed to the aggressive cost controls implemented by corporations and the private sector well in advance of the ensuing slowdown. Thus, while non-financial corporate earnings, cash flows and balance sheets have exited this recession in relatively strong condition, employment and production have borne the brunt of the slowdown. As a result of lower activity levels, constrained end market demand and excess manufacturing capacity, core inflation trends as measured by the consumer and producer price indices of the Department of Labor have remained relatively subdued. The exception has been select commodity prices, which have been influenced by global demand factors and supply and demand considerations related to particular commodities.

28. The Canadian economy has also experienced a sharp recovery from the cycle trough levels of 2009. Real inflation-adjusted Canadian gross domestic product (GDP) growth of 0.6 per cent, according to Statistics Canada, for the month of March 2010 compared with a negative 0.9 per cent reading at the cycle low of December 2008. On a year-over-year basis, March GDP advanced 3.1 per cent compared with a negative 4.1 per cent reading in July 2009. The first quarter 2010 implied GDP growth of 6.1 per cent inflation-adjusted (annualized) represents the highest pace of economic growth since September 2000. At the trough of the recent recession, the Canadian economy contracted at a near 7 per cent annual rate (March 2009). Consistent domestic manufacturing output, a recovery in consumer spending, a balanced housing market and a strong financial (banking) sector have largely placed the Canadian economy in a relatively strong global position. Also, a recovery in worldwide commodity prices aided the Canadian economy, as a significant

portion of output and exports is resource-related. Although unemployment was high by historical standards (8.2 per cent as at March 2010), it has likely reached its peak level for this cycle, which was an 8.7 per cent reading in August 2009.

29. The most dramatic consequence of this period has concerned the reshaping of the global financial sector. Noteworthy because of the widespread effect that this recent experience has had on the real economy, the systemic "shock" related to liquidity and solvency concerns among various financial entities is still being rationalized through the global financial system. Aggressive and unprecedented steps by fiscal and monetary authorities in conjunction with the policy initiatives of governmental bodies narrowly allowed the financial system to survive stresses of the 2008-2009 financial crisis. The implications of such moves are yet to be fully recognized as the complex interaction of the financial sector and the global economy continues to evolve. This is still a "work in progress" that merits close and cautious scrutiny, as risks continue to be present that may derail the present global economic recovery.

30. The fiscal year ending on 31 March 2009 began with concerns about rising inflation as commodity prices, especially oil, continued to soar. There were also signs of a slowing European economy, with declining consumer and business confidence. Inflation in Europe reached 4 per cent by June 2008, exceeding the 2 per cent ceiling. The European Central Bank was concerned enough about inflation that it raised interest rates by 25 basis points. At the beginning of the third quarter of 2008, the economic outlook for Europe was tempered when the euro-area economy contracted for the first time in almost 10 years. Moreover, global confidence in the financial system collapsed with the bankruptcy of Lehman Brothers in an already fragile financial system. In Europe, this led to the nationalization of several banks. Sovereign loan guarantees for banks were needed to instil confidence in the banking system. The severity and duration of the frozen credit market, in conjunction with slowing global demand, caused Europe to enter into a recession by midyear. Countries in Europe responded individually with stimulus packages ranging from 1.5 per cent to 4.4 per cent of GDP during the 2008 to 2010 period. Job security also weighed on consumers, although less so in countries with stronger social safety nets, as companies focused on cost reduction and cash preservation. By the fourth quarter of 2008, the unemployment rate had reached 8.5 per cent in the euro region and 6.5 per cent in the United Kingdom of Great Britain and Northern Ireland. As the threat of inflation receded and growth expectations reduced, the Bank of England and the European Central Bank lowered interest rates to stimulate lending and business activities. By March 2009, the European Central Bank and the Bank of England lowered interest rates to low levels of 1.5 per cent and 0.5 per cent, respectively. During the fiscal year, the euro weakened 16.3 per cent versus the United States dollar, to $1.32 from $1.58, and the British pound weakened 28.0 per cent against the United States dollar, to $1.43 from $1.98.

31. The fiscal year ending March 2010 was characterized as a gradual economic recovery from the financial crisis, supported in large part by Government stimulus packages and accommodating monetary policies. During the first half of the fiscal year, signs of the European economy bottoming out emerged as economic data improved and credit access eased. Consumer confidence and investor sentiment improved with better access to credit, accelerated implementation of public spending and muted inflation. Unemployment rates continued to rise, however, and underlying demand growth was weak. By August of 2009, unemployment rates had

climbed to a decade high in the euro zone and the United Kingdom, at 9.6 per cent and 7.9 per cent, respectively. During this period, the European Central Bank lowered its main lending rate to 1 per cent, while the Bank of England maintained its bank rate at 0.5 per cent. In addition, both Banks implemented extraordinary asset purchase programmes to provide further liquidity to the market. By the end of the first half of the fiscal year, as a result of Government stimulus and policies, most economies in Europe had exited the recession. The recovery momentum extended into the second half of the fiscal year, with some indicators surpassing pre-Lehman levels. Despite the improving trends, the sustainability of the recovery was uncertain, owing to the effects of inventory restocking and stimulus packages still working their way into the economy. Unemployment remained at high levels. While the central banks acknowledged the fragility of the recovery and maintained historic low lending rates, the European Central Bank announced its intention to phase out the extraordinary measures taken during the crisis so as not to cause inflationary pressure. Towards the end of the fiscal year, the European economy seemed to be on the path of gradual recovery, but the focus of the market turned to the highly indebted countries within the European Union. Sovereign default risks rose, with record spreads between Government bonds in Europe not seen since the formation of the European Union. The euro exchange rates against other currencies were under severe pressure, as the cohesiveness of the European Union was in doubt by the market. The European Union, with co-financing from the International Monetary Fund, created packages of last-resort credit facility totalling up to 750 billion euros, which will be available for the next three years to its members and contingent upon the borrower agreeing to additional deficit reduction measures. During the fiscal year, the euro was volatile, rising to a high against the United States dollar of $1.51 on 25 November as the economic recovery gained momentum and later declining to a low of $1.33 on 25 March as concerns about sovereign risks mounted. Similarly, the British pound rose against the United States dollar to a high of $1.70 on 5 August and started a declining trend in November, with increasing worries about the outcome of the election, to $1.52 by 31 March 2010.

32. The global financial crisis led to a severe downturn in the Japanese economy in fiscal year 2008; however, Japan benefited from the turnaround in global economies led by the strong recovery in emerging markets, especially China, through fiscal year 2009. Confidence among Japan's large manufacturers declined, with the Bank of Japan's Tankan survey diffusion index falling from 5 in June 2008 to -58 in March 2009, the worst figure since the survey started in 1974. The magnitude of decline narrowed after that time, however, to -14 in March 2010. Various stimulus measures in major countries boosted demand for durable goods such as automobiles and televisions, which worked favourably for exports from Japan. The monthly export value from Japan, which had dropped year over year since October 2008 and recorded a 49 per cent decline in February 2009, turned positive in December 2009, and has been growing 20 to 40 per cent year over year in 2010. Industrial production also turned to positive growth in December 2009 for the first time in 14 months and posted 32 per cent year-over-year growth in March 2010. Gross domestic product rose year over year in the first quarter of 2010 after seven consecutive quarters of decline. Domestic demand has yet to show a clear sign of recovery, however, with unemployment still high at 4.9 per cent in March 2010 and domestic capital expenditure still at a low level. Although the Bank of Japan showed its commitment to combating deflation by implementing quantitative easing, the core consumer price index (CPI) has remained in negative territory since

February 2009. Through the biennium ending March 2010, the yen strengthened against major currencies. Against the United States dollar, the yen strengthened from 108.80 yen in August 2008 to 86.41 yen by the end of March 2010. The yen appreciated even more sharply against the euro, from 168.39 yen in July 2008 to 121.26 yen in February 2010.

33. During the biennium ended March 2010, the Australian economy performed better than most developed economies by avoiding recession throughout the global financial crisis. Aggressive monetary and fiscal policy action supported the domestic economy, while China's own economic stimulus measures led to strong demand for commodities from Australia. The Australian Government distributed 12 billion Australian dollars ($A) to households and spent $A 22 billion on infrastructure projects. The Reserve Bank of Australia began lowering its benchmark cash lending rate in September 2008; by May 2009, the rate had been reduced by a total of 425 basis points, to a 49-year low of 3.0 per cent, in an effort to prevent economic recession. In November 2009, the Reserve Bank of Australia became the first Group of Twenty (G-20) central bank to begin raising interest rates as economic data provided evidence that economic growth had begun to accelerate in response to the accommodative fiscal and monetary policies. Growth in GDP rebounded to 2.7 per cent year over year in the first quarter of 2010 after weakening to a low of 0.9 per cent in the first quarter of 2009 from 3.3 per cent in the first quarter of 2008. The unemployment rate rose from 4.0 per cent in March 2008 to a peak of 5.8 per cent in June 2009 and fell to 5.3 per cent by March 2010. The Australian CPI fell 2.9 per cent year over year in the first quarter of 2010 after peaking at an increase of 5.0 per cent in the third quarter of 2008 and compared with an increase of 4.2 per cent in the first quarter of 2008. The CPI is within the Reserve Bank of Australia's comfort range of 2 per cent to 3 per cent. The Australian dollar appreciated 0.55 per cent versus the United States dollar during the biennium.

34. The GDP of Hong Kong SAR contracted 2.7 per cent year over year in fiscal year 2008 as a result of the global financial crisis, and rebounded in fiscal year 2009 with 2.5 per cent year over year growth as the global economy recovered, led by China and other emerging markets. Residential property prices continued on an upward trend, supported by low interest rates, a supply shortage, good affordability and mainland Chinese demand. The CPI in Hong Kong SAR rose by 2.0 per cent year over year in March 2010, rebounding from a low of -1.6 per cent in August 2009. Retail sales rose sharply after contracting for seven consecutive months from February 2009 to August 2009, with growth accelerating from 2.4 per cent year over year in September 2009 to 19 per cent in March 2010. Singapore's GDP contracted 4.2 per cent year over year in fiscal year 2008 and rose 4.0 per cent in fiscal year 2009 as the global economic recovery led to a surge in non-oil domestic exports. After contracting for 18 consecutive months from May 2008 to October 2009, non-oil domestic export growth accelerated from 8.7 per cent year over year in November 2009 to 25.4 per cent in March 2010. The Singapore dollar depreciated 1.4 per cent against the United States dollar during the biennium.

35. During the biennium ending March 2010, economies in the emerging countries experienced significant volatility. In the early part of the period, emerging countries were heavily impacted by the sharp economic deterioration of the developed economies. The latter part of the biennium was characterized by a synchronized recovery, owing mainly to an unprecedented level of fiscal stimulus policies. The

rate of economic growth of emerging and developing economies declined from 6.1 percent in 2008 to 2.5 percent in 2009 before recovering in early 2010.

36. In emerging Asia, China remained the fastest growing economy, with GDP growth of 9.6 per cent in 2008 and 9.1 per cent in 2009, mostly resulting from a stimulus package in the amount of 4 trillion yuan. Quarterly growth in GDP dropped to 6.2 per cent in the first quarter of 2009 before recovering to 11.9 per cent in the first quarter of 2010. Exports experienced a significant contraction in 2008, but have since improved. Other economic data such as industrial production, retail sales and urban fixed-asset investment remained strong or also recovered in early 2010. During this period, China became the world's largest auto market and overtook Germany as the world's biggest exporter. Money and credit indicators that declined last year, giving the central bank some room to cut interest rates, are now pointing to a growing risk of economic overheating. The authorities have implemented more restrictive bank lending and housing policies while reinstating the need to focus on gradually reforming the exchange-rate mechanism. China is a high priority for the Fund. During the 205th meeting of the Investments Committee, meetings were held in Beijing with top economists and regulatory officials, with the aim of determining what additional investments would be prudent in the very dynamic China A-shares market. The Fund currently holds shares listed in Hong Kong SAR rather than in Shanghai. These meetings established a formal and unparalleled bridge of communication and forum for the Fund and the Government of China. Moreover, it gave the Investments Committee the opportunity to assess the plans of the authorities to generate social and economic progress. The A-shares market is now the major place for Chinese companies to raise funds, and its broad array of equities should provide the Fund with substantial investment prospects.

37. A similar high priority, India maintained a relatively high level of economic growth during the period under review. India's GDP grew 6.4 per cent in 2008, moderated to growth of 5.7 per cent in 2009 and accelerated again as rising incomes boosted consumer demand for cars, mobile phones and air travel, while exports rose on the back of the global recovery. Salaries in India may increase at the fastest pace in the Asia-Pacific region in 2010. Headline inflation, measured by the wholesale price index, rose to 9.89 per cent as food prices soared and taxes on crude oil and refined products increased. Fear of higher inflation has prompted India's central bank to increase interest rates.

38. The Republic of Korea was severely impacted by the slump in the global demand because of its heavy reliance on exports, which accounted for 60 per cent of the economy. The Korean won experienced a sharp decline as exports contracted. Rising unemployment also prompted consumers to pare spending. The economy recovered in the first quarter of 2010 as the global recovery spurred demand for electronics. Recovery in private consumption followed, and manufacturer confidence rose to the highest level in more than seven years. The won has since recovered back to near the pre-crisis level. While inflation remained benign, the Bank of Korea maintained its benchmark interest rate of 2 per cent to encourage corporate and consumer spending.

39. In Latin America, Brazil's GDP contracted by 0.2 per cent in 2009 after rising 5.1 per cent in 2008. During the fourth quarter of 2008, the economy deteriorated as companies reduced employment and sales forecasts in anticipation of slower demand and tighter credit. The Government responded with cuts in sales taxes on

durable goods and pledges to sustain public work projects, while the Central Bank cut its overnight lending rate. The recovery that started at the end of 2009 highlighted that aggressive fiscal policies effectively stimulated consumer spending and fixed-asset investments. Gross domestic product increased 9.0 per cent in the first quarter of 2010, with retail sales rising 9.1 per cent, the most since 2001. More recently, the authorities, in a move to slow down the rapidly expanding economy and control accelerating inflation, raised the benchmark Selic rate to 10.25 per cent. Mexico also suffered economic contraction because of its high correlation with the United States business cycle. Gross domestic product contracted severely, from an increase of 1.5 per cent in 2008 to a decrease of 6.5 per cent in 2009.

40. Mexico's GDP expanded 9.9 per cent year over year in the first quarter of 2010 as a rebound in United States manufacturing increased demand for Mexican exports. The increase in CPI recently reached 4.3 per cent, but the Bank of Mexico kept its benchmark interest rate unchanged at 4.5 per cent. In Chile, the economy slowed as the recession in developed markets reduced demand for copper, the country's biggest export. The economy recovered to a positive growth level of 2.1 per cent by the fourth quarter of 2009, owing to record low lending rates and improving global demand for commodities.

41. During the period under review, Eastern European economies experienced the highest level of volatility among the emerging countries. The economy of the Russian Federation decelerated, mainly because of falling commodities prices, and the ruble sharply depreciated. Russian Federation GDP declined 7.9 per cent in 2009 from an increase of 5.6 per cent in 2008, but rose 2.9 per cent in the first quarter of 2010, along with a rebound in energy and metals prices. The Russian central bank lowered its key interest rate to a record low of 7.75 per cent. Other economies in the Europe, Middle East and Africa region, such as Hungary, the Czech Republic, Poland and Turkey, suffered from a reduction in capital flows, high current account deficits and defensive monetary policy. Their industrial production slumped as the global financial crisis choked investments and recession in Western Europe cut export demand. Eastern European economies started to recover as from the end of 2009, as industrial output increased on rising manufacturing orders from European Union countries. The economy in Turkey managed to deal with the economic shock without a request for external aid, and rebounded strongly as decreased unemployment and private consumption recovery begin to solidify. In South Africa, manufacturing fell as the global recession slashed demand for exports and lowered output from the automotive and non-ferrous sectors. Although the employment level remained a significant challenge in South Africa, most economic data showed that the country had emerged from its recession. Growing global export demand is boosting South African manufacturing output, including metals, which account for a large part of the economy.

42. In summary, emerging market economies experienced a contraction followed by a recovery driven by supportive monetary and fiscal policies. As the worst of the global economic crisis is behind us, the coming year may be challenging, as fiscal stimulus programmes are winding down and the threat of inflation could lead to rising interest rates. Emerging countries have been the major drivers and beneficiaries of the economic prosperity of the past decade. It is expected that they will continue to experience faster economic growth for some years to come. While the regions are not all on the same standing, they generally benefited from political stability, better policy frameworks, institutional reforms and improved governance.

Most countries have credible monetary policies and strong reserve positions. With global trade liberalization and market deregulation, the export-led emerging economies have accumulated sizable trade surpluses, while industrialized countries are faced with growing current account deficits. Although the situation has improved over the last couple of years, the preconditions for private sector development over the next decade remain better governance at both governmental and corporate levels as well as more efficient judicial systems. Longer term, as more emerging markets reach the critical economic mass to decouple somewhat from the developed economies, global emerging markets should continue their upward trend based on positive fundamentals. The Fund expects to remain overweight in emerging markets.

43. During the biennium ended 31 March 2010, the fixed income portfolio was faced with a historically severe credit crisis followed by massive Government intervention and growing concerns about sovereign funding. In 2008, problems in the United States mortgage market and among asset-backed securities grew into a full-blown global financial meltdown. Lehman Brothers collapsed and the Government of the United States put the mortgage giants Fannie Mae and Freddie Mac into conservatorship. Financial institutions around the world faced a liquidity crunch on top of an economic recession. Investors sought the relative safety of Government bonds and the perceived safe haven of the United States dollar. In response to the crisis, central banks aggressively reduced policy rates and implemented asset purchase programs while Governments launched huge stimulus programmes, including guarantees and capital injections for ailing banks. The results of these efforts were seen during the course of 2009. Slowly, confidence started to return in the banking sector and capital markets reopened. Economic activity bottomed out and recovered, albeit tentatively. Bond markets stabilized and beaten-down sectors, such as corporate bonds, rallied. As the period closed, however, the impact of the credit crisis lingered. Early in 2010, bond markets reflected concerns over sovereign credits after Governments had issued unprecedented amounts of debt to fund their recovery programmes. The fixed-income markets are likely to remain volatile, as the pace of the economic recovery is resolved and the level of fiscal support to spur growth is balanced against sovereign debt loads.

44. During the biennium ended 31 March 2010, commercial real estate markets saw an acceleration of the slowdown in investment activity that had begun during the credit crunch of 2007. With the collapse of Lehman Brothers in September 2008, real estate valuations dropped significantly in the third and fourth quarters of 2008. Drawdowns of capital by fund managers changed from an average of $80 million per quarter prior to the fourth quarter of 2008 to an average of $40 million per quarter during 2009 and the first quarter of 2010. New commitments to real estate funds ceased in August 2008, and only one small commitment was made during the rest of the biennium, in December 2009. The focus of the Investment Management Division during this biennium has been on the asset management of its existing funds, culminating in the replacement of one of its fund managers in Japan and the restructuring of its relationships with two other managers.

45. New investment underwriting activity began in the first quarter of 2010, focusing mainly on investments in Japan and Asia. Real estate markets continued a schism that began in 2009, separating high-growth markets such as China, India and Brazil from low-growth markets such as Japan, the United States and Europe. The high-growth markets continue to focus on real estate development, and the low-growth markets centre on distress, mostly on real estate investments trapped in

poorly capitalized banks. Expectations of a return to growth in Japan, the United States and Europe were muted at the end of the biennium, resulting in a continued decline in real estate values, which discouraged investments in that area.

IV. Diversification

46. Diversification is the investment of assets among a variety of securities or among securities in a variety of markets with the goal of controlling risk in a portfolio without proportionately reducing the expected return. The Fund's policy of broad diversification of its investments by currency, types of asset classes and geographical areas continues to be the reliable method of improving the risk-return profile of the Fund's portfolio over long periods of time. The Fund is unique among major pension funds in its commitment to diversifying its portfolio on a fully global basis.

47. During the biennium ended 31 March 2010, exposure to equities was kept below the neutral 60 per cent long-term strategic guideline through 30 June 2009 but above the 60 per cent strategic guideline as the global economy was on the path of recovery. Equities were at 65.6 per cent at the end of the biennium. Bonds were kept well above the 31 per cent long-term strategic target guideline, beginning the biennium at 36.7 per cent of the portfolio and decreasing to 28.6 per cent at the end of March 2010. Exposure to real estate declined from 4.4 per cent of the portfolio on 1 April 2008 to 3.6 per cent at the end of the biennium. Cash and short-term investments started the biennium at 1.8 per cent in April 2006 and ended the biennium at 2.2 per cent. The investment portfolios are continually being rebalanced following the quarterly meetings of the Investments Committee in order to achieve the tactical asset allocation decided by the representative of the Secretary-General. During fiscal year 2010, the equity portfolio generated more income than the bond portfolio. The combination of high capital appreciation from equities and high income from bonds has been beneficial to the Fund. Investments in only one asset class would have been detrimental to the performance of the Fund since diversification of risk would not have been achieved.

48. In addition to changes to the proportions of the various asset classes in the portfolio, changes were made within asset classes in order to implement the Fund's investment strategy and take advantage of new trends in economic cycles and financial markets. By the end of fiscal year 2010, United States equities were kept in line with the benchmark when compared with the underweight position at the end of fiscal year 2009. The exposure to European equities was reduced and was kept almost in line with the benchmark by the end of fiscal year 2010 because of concerns about the fiscal situation in the region, particularly in Greece, Spain, Italy and Portugal. Investments in emerging market equities were increased during the biennium and benefited from strong performance results. Developing markets such as India and China continued to grow much faster than developed countries. The Fund maintained a modest underweight in the financial sector and continued to limit exposures, particularly from the third quarter of 2007 onwards. For the biennium, the Fund maintained overweight in the materials and industrial sectors. The relative overexposures and underexposures have contributed positively to the Fund's overall performance. This broad diversification of the Fund reduces risk across currencies and markets.

49. The fixed-income portfolio is invested in 16 different currencies, 42 per cent of it in United States dollars and 58 per cent in non-dollar currencies. United States-dollar denominated bonds comprise 11.9 per cent of the entire portfolio. In terms of geographical diversification, the fixed-income portfolio was invested in 28 countries and 5 supranational and regional institutions as at March 2010.

50. In terms of geographical diversification, the proportion of the Fund invested in North America increased from 36.3 per cent in March 2008 to 43.1 per cent in March 2010. Investments in Europe decreased from 36.0 per cent to 29.3 per cent, while the proportion of investments in Asia and the Pacific decreased from 20.4 per cent to 18.5 per cent during the movements in currencies and interest rates. During the market recovery, the United States dollar fluctuated against most currencies worldwide; the currency effect from investments in the euro, the Japanese yen and Latin American securities reduced the overall Fund risk and increased the total return for the same period. With geographic changes, currency diversification also changed. Diversification in terms of asset class, currency and region had a significant impact on the performance of the Fund. Investing in only one currency other than the United States dollar would have had a negative impact on the performance, as movements of currencies against the dollar are not synchronized. There were several times when the total returns were negative in local currencies but positive in dollar terms. Areas of the Fund's investment are shown in tables 1 through 3.

Table 1
Market value of Fund investments by country or area as at 31 March 2010[a]

Country/area	*Amount (in millions of United States dollars)*	*Percentage*
Albania[b]	—	—
Australia	1 259.0	3.28
Belgium	139.5	0.36
Brazil	571.7	1.49
Canada	1 657.6	4.32
Chile	45.5	0.12
China	1 141.0	2.98
Colombia	4.8	0.01
Czech Republic	45.1	0.12
Denmark	125.6	0.33
Egypt	17.2	0.04
Estonia	33.1	0.09
Finland[b]	—	—
France	1 979.0	5.16
Georgia[b]	—	—
Germany	1 553.2	4.05
Greece	111.6	0.29
Hungary	58.6	0.15
Iceland	21.9	0.06
India	302.5	0.79

Country/area	Amount (in millions of United States dollars)	Percentage
Ireland	102.7	0.27
Italy	229.0	0.60
Japan	2 751.2	7.17
Latvia[b]	—	—
Lithuania	32.6	0.09
Malaysia	562.9	1.47
Mexico	593.3	1.55
Netherlands	394.2	1.03
New Zealand	10.7	0.03
Norway	526.3	1.37
Poland	492.5	1.28
Portugal[b]	—	—
Qatar	10.5	0.03
Republic of Korea	795.9	2.08
Republic of Moldova[b]	—	—
Russian Federation	297.4	0.78
Singapore	253.7	0.66
South Africa	350.5	0.91
Spain	715.5	1.87
Sweden	552.2	1.44
Switzerland	1 241.3	3.24
Turkey	110.8	0.29
Ukraine[b]	—	—
United Kingdom	2 478.7	6.46
United States	14 896.0	38.84
Venezuela (Bolivarian Republic of)	24.0	0.06
Emerging markets[c]	37.0	0.10
International[c]	900.3	2.35
Regional Africa	157.7	0.41
Regional Asia	249.4	0.65
Regional Europe	444.5	1.16
Regional Latin America	44.0	0.11
Regional Middle East	15.8	0.04
Euro[c]	10.4	0.03
Total fund	**38 347.8**	**100.00**

[a] Country of investment is generally based on domicile of issuer. Convertible securities are classified in accordance with the security into which they are convertible.

[b] Countries with investments in real estate with less than 0.01 per cent of the Total Fund.

[c] Emerging markets and euro funds are invested in a number of countries under the particular area or currency. International refers to investments in international development institutions, such as the World Bank.

Table 2
Fund investments in developed markets

Country	Equities		Fixed income	
	31 March 2008	31 March 2010	31 March 2008	31 March 2010
Australia	√	√	√	√
Austria	—	—	√	—
Belgium	√	√	√	√
Canada	√	√	√	√
Denmark	√	√	√	—
Finland	√	—	—	—
France	√	√	√	√
Germany	√	√	√	√
Greece	√	√	—	—
Iceland	—		√	—
Ireland	√	√	√	√
Israel	√	√	—	—
Italy	√	√	√	—
Japan	√	√	√	√
Netherlands	√	√	√	√
New Zealand	—	√	—	√
Norway	—	√	√	√
Portugal	—	—	√	—
Singapore	√	√	√	√
Spain	√	√	√	—
Sweden	√	√	√	√
Switzerland	√	√	√	√
United Kingdom	√	√	√	√
United States	√	√	√	√
Total	**19**	**20**	**20**	**15**

Table 3
Fund investments in emerging markets

Country	Equities[a]		Fixed income	
	31 March 2008	31 March 2010	31 March 2008	31 March 2010
Argentina	√	—	√	√
Angola			—	√
Bahrain	√	√		
Bosnia and Herzegovina			—	√
Botswana	√	√	—	—
Brazil	√	√	√	√
Bulgaria	√	—		

	Equities[a]		*Fixed income*	
Country	*31 March 2008*	*31 March 2010*	*31 March 2008*	*31 March 2010*
Cayman Islands			—	√
Chile	√	√	√	√
China	√	√	√	√
Colombia	√	√	√	—
Congo	√	—		
Côte d'Ivoire	—	—	√	√
Croatia			—	√
Cyprus	—	—	√	—
Czech Republic	√	—	√	√
Democratic People's Republic of Korea			—	√
Dominican Republic			√	√
Ecuador			√	√
Egypt	√	√	√	√
El Salvador			√	√
Estonia	—	—	√	√
Fiji			√	√
Georgia			—	√
Ghana	√	√	√	√
Grenada			√	√
Hungary	√	√	√	√
India	√	√	—	—
Indonesia	√	—	√	—
Iraq			√	√
Israel			—	—
Jordan	√	√	√	√
Kazakhstan	√	—	√	√
Kenya	√	√		
Kuwait	√	√		
Kyrgyzstan	√	—		
Lebanon	√	√		
Lithuania	—	—	√	√
Malawi	—	√	√	√
Malaysia	√	√	√	√
Marshall Islands	√	—		
Mauritius	√	√	—	—
Mexico	√	√	√	√
Morocco	√	√	—	—
Namibia	√	√		
Nepal			√	—
Nigeria	√	√	√	√
Oman	√	√	—	—

Country	Equities[a]		Fixed income	
	31 March 2008	31 March 2010	31 March 2008	31 March 2010
Pakistan	—	—		
Palestine	√	√		
Panama	√	—		
Peru	√	—	√	—
Philippines	√	—	—	√
Poland	√	√	√	√
Qatar	√	√	√	√
Republic of Korea	√	√	√	√
Republic of Moldova			√	—
Russian Federation	√	√	√	√
Saudi Arabia	—	√		
Senegal	√	√		
Serbia			√	—
South Africa	√	√	√	√
Sri Lanka	—	—		
Thailand	√	—		
The former Yugoslav Republic of Macedonia			—	√
Trinidad and Tobago			√	√
Tunisia	√	√		
Turkey	√	√	√	√
Turkmenistan	√	—		
Ukraine	√	—	√	√
United Arab Emirates	√	√		
Uruguay			√	√
Venezuela (Bolivarian Republic of)	√	—	√	√
Viet Nam	√	—	√	—
Zambia	√	√	√	√
Zimbabwe	√	√		
Total	**49**	**35**	**42**	**42**

[a] The sale of the externally managed Emerging Markets Investors Fund in July 2008 as a result of its underperformance has led to a reduction in the number of developing countries in which the Fund is currently invested. Please note that on 30 June 2010 the Investment Management Division signed a contract with the African, Latin American and Caribbean Fund, a private equity fund managed by International Finance Corporation Asset Management Company. The Investment Management Division is seeking more opportunities to invest in emerging markets.

V. Investment returns

A. Total return

51. The market value of the Fund's assets decreased from $40,588 million on 31 March 2008 to $38,348 million on 31 March 2010, a decrease of $2,240 million or approximately 6.0 per cent. The total investment return was -28.30 per cent for the year ended 31 March 2009 and 32.20 per cent for the year ended 31 March 2010. After adjustment by the United States CPI, these returns represent real rates of return of -28.1 per cent and 29.2 per cent, respectively. The total annualized rate of return for the biennium was, therefore, -2.65 per cent.

52. Following the rebalancing of the portfolio in 2009, the Fund earned 32.2 per cent for the fiscal year ending 31 March 2010. This was the highest annual return in the history of the Fund. United States equity returned -34.6 per cent in fiscal year 2009 and 42.6 per cent in fiscal year 2010. Non-United States equity returned -45.1 per cent in 2009 and 62.2 per cent in 2010. Equities represented 51.9 per cent and 65.6 per cent of the total Fund in 2009 and 2010, respectively. Total equities returned 41.0 per cent in 2009 and 54.1 per cent in 2010. In 2010 equities denominated in currencies other than the United States dollar had a weaker impact on the performance since the United States dollar appreciated against major currencies. United States bonds showed returns of -1.4 per cent in 2009 and 5.9 per cent in 2010. Non-United States bonds returned -12.6 per cent in 2009 and 16.7 per cent in 2010. Real estate performance was -22.9 per cent in 2009 and -17.4 per cent in 2010. Short-term investments returned 3.9 per cent in 2009 and -2.7 per cent in 2010.

53. The rates of return shown in the present report have been calculated by an outside master record-keeper, using a generally accepted method that was elaborated in the report on the management of the investments submitted to the Board at its thirty-fourth session.[1] The calculation includes actual income received from dividends and interest as well as realized capital gains and losses. It also takes into account changes in the market value of the investments and the timing of cash flows.

B. Comparisons of investment returns

54. The Fund continues to be, geographically, the most widely diversified pension fund that maintains its accounts in United States but has liabilities in several other currencies. At the end of the period under review, the Fund had more than 50 per cent of its assets in currencies other than the United States dollar.

55. During the year ended 31 March 2009, the Fund outperformed the new policy benchmark, which is comprised of 60 per cent Morgan Stanley Capital International (MSCI) All Country World Index, 31 per cent Barclays Capital Global Aggregate Bond Index, 6 per cent National Council of Real Estate Investment Fiduciaries (NCREIF) Open-End Diversified Core Equity Index and 3 per cent Merrill Lynch 91-day Treasury bill, with a return of -28.3 per cent versus 29.8 per cent for the policy benchmark. For the year ended 31 March 2010, the Fund underperformed the

[1] JSPB/34/R.10.

benchmark, with a return of 32.2 per cent versus the return of 33.7 per cent of the new 60/31 benchmark. Over the last 15 years, the Fund has achieved an annualized return of 7.7 per cent, outperforming the 6.5 per cent return of the 60/31 benchmark. For the fiscal year ending 31 March 2010, the total fund increased by 32.2 per cent. In particular, the equity of emerging markets rallied strongly, by more than 80 per cent, and the Fund's overweighted position in global emerging markets contributed positively to the performance; however, the Fund slightly underperformed the 60/31 benchmark by 1.5 per cent owing to the Fund's conservative approach to constructing the portfolio. The Fund remained deliberately underweight in financials during the financial crisis, and the relative underperformance is a reflection of the rally in the lowest tier of banking institutions, in which companies that seemed on the verge of death managed to survive the crisis. In the earlier years, the Fund underperformed mainly as a result of its low weighting in equities, but the Fund has caught up rapidly since 2000 owing to outperformance in equities and bond asset classes.

56. Over the last 15 years, the MSCI All Country Index and the MSCI World Index had a total annualized return of 6.6 per cent and 6.4 per cent, respectively, compared with the annualized return of 7.7 per cent achieved by the Fund's equity asset class. During the same period, the Barclays Capital Global Aggregate Index and the Citigroup World Government Bond Index had annualized returns of 6.1 per cent and 5.7 per cent, compared with the annualized return of 6.3 per cent achieved by the Fund's bond portfolio.

57. **Risk management.** The diversification of the Fund and its conservative practice of investing in higher quality companies have continued to protect the Fund. The Investment Management Division has, with the assistance of the Procurement Division, expanded its risk management information services, and has conducted a request for proposal to build this capability further. As for staffing, the Investment Management Division has hired a deputy director for risk management.

58. **Infrastructure improvements.** As stated above (see paragraph 10), in January 2010 the Investment Management Division inaugurated the use of an electronic trade order management system and integrated it with the secure SWIFT financial telecommunications system, which went live at the time of the last Pension Board meeting. The P-5 Senior Information Systems Officer was recruited and given this project as a top priority in July 2008. With improved infrastructure, the Fund is now a safer client, meeting the highest industry standards.

59. **Alternative asset classes.** The Investment Management Division presented a report regarding the addition of alternative asset classes to the portfolio. The report, which was prepared by Mercer Investment Consulting, Inc., recommended the incorporation of private equity and hedge funds of funds into the portfolio, because the implementation of those additional asset classes would reduce the overall risk of the portfolio, as measured by standard deviation, while improving the return. The Investment Management Division has hired a senior investment officer for alternative investments, and has also signed a contract with a private real asset adviser to provide guidance regarding infrastructure funds and agricultural and timber lands.

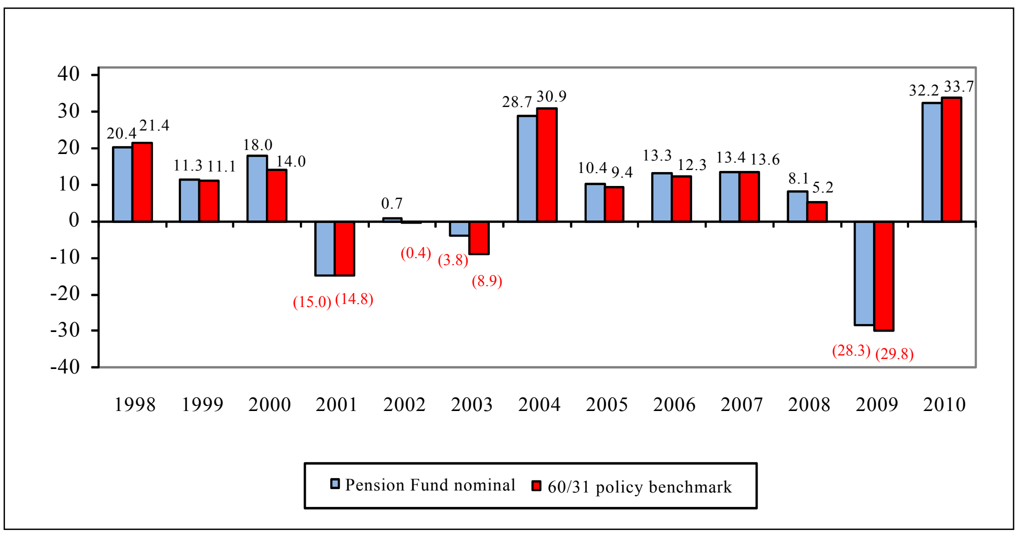
60. The Board noted the Investment Management Division's need for appropriate resources for environmental, social and governance research and proxy voting services in order to effectively support the implementation of the principles, and

expressed interest in reviewing detailed implementation plans for the following year. As evidence of its commitment, following a lengthy and rigorous due diligence process, the Fund signed an agreement with the International Finance Corporation committing the Fund to a private equity stake of $150 million in its African, Latin American and Caribbean Fund, which incorporates the Secretary-General's environmental, social and governance issues in the investment analysis. The African, Latin American and Caribbean Fund is a private equity fund with up to $950 million in commitments raised by the International Finance Corporation Asset Management Company, a wholly-owned subsidiary of the International Finance Corporation, to make equity investments in growth companies located in developing countries in Africa, Latin America and the Caribbean. In 2008, when the World Bank launched the strategic framework for development and climate change to help stimulate and coordinate public and private sector activity to combat climate change, the Pension Fund participated in the initial issuance of World Bank Green Bonds, as well as subsequent offerings.

C. Long-term rates of return

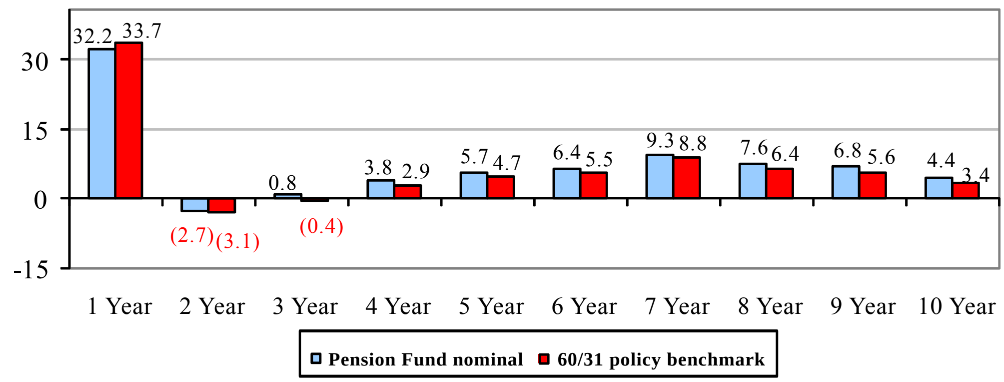
61. During the biennium ended 31 March 2010, the Fund encompassed the most volatile markets in its history. Historically, equity markets had strong positive returns from 1993 to 2000, but declined sharply in the following three consecutive years. For 2008, 2009 and 2010, the Fund's returns were 8.1 per cent, -28.3 per cent and 32.2 per cent, respectively (see figure I).

Figure I
Fiscal year returns through 31 March: nominal return of the Fund outperforms policy benchmark in 8 out of 13 periods



62. The annualized total returns for the past 5, 10, 15, 20 and 25 years were approximately 5.7 per cent, 4.4 per cent, 7.7 per cent, 8.1 per cent and 9.8 per cent, respectively. As illustrated in figure II, the Fund exceeded the policy benchmark in 9 out of the 10 rolling year periods through 31 March 2010. The annualized total rate of return over the 50-year period for which data was available was 8.3 per cent, representing a yearly real rate of return of 4.1 per cent after adjustment by the United States CPI.

Figure II
Rolling year performance through 31 March 2010: nominal return of the Fund exceeds the policy benchmark in 9 out of 10 periods



UNJSPF Nominal return exceeds the 60/31 Policy Benchmark in 9 out of 10 periods

Table 4
Fund annual total rate of return
(Percentages based on market value as at 31 March)

	Equities				*Bonds*						
Year	*United States*	*Outside United States*	*Total*	*MSCI World Index*[a]	*United States*	*Outside United States*	*Total*[b]	*CWG Bond Index*[c]	*Real estate*	*Short term*	*Total Fund*
1961	18.8	37.8	19.4	—		—	8.0	—	—	—	12.7
1962	12.37	0.87	11.65	—	—	—	3.91	—	—	—	6.61
1963	(0.60)	(16.34)	(0.59)	—	—	—	5.49	—	—	—	4.07
1964	18.18	7.48	17.45	—	—	—	2.12	—	—	—	8.24
1965	10.89	8.30	10.44	—	—	—	4.41	—	—	—	6.98
1966	4.53	3.22	4.31	—	—	—	(2.14)	—	—	—	0.66
1967	11.76	(2.32)	8.98	—	—	—	3.97	—	—	—	7.91
1968	2.86	28.30	7.46	—	—	—	(4.89)	—	—	—	1.60
1969	13.35	20.07	14.64	—	—	—	2.66	—	—	—	9.09
1970	(5.10)	(2.18)	(4.49)	—	—	—	1.41	—	—	—	(1.75)
1971	13.94	3.31	11.46	9.28	—	—	14.10	—	—	8.73	13.53
1972	14.13	34.30	18.33	16.92	—	—	9.41	—	11.58	7.15	16.98
1973	5.85	20.77	9.49	13.47	—	—	7.40	—	4.78	5.92	8.55
1974	(16.70)	(21.48)	(18.10)	(16.40)	—	—	1.92	—	10.18	10.70	(13.55)
1975	(11.20)	11.60	(5.16)	(6.09)	6.20	14.63	6.55	—	(1.03)	12.35	0.18
1976	16.37	10.76	14.58	15.59	11.22	1.91	10.02	—	5.16	7.70	13.16
1977	(8.25)	(3.75)	(6.62)	(0.95)	10.40	15.20	11.06	—	3.70	5.20	(0.26)
1978	(5.60)	20.31	4.16	6.11	5.62	24.39	8.72	—	8.25	7.67	6.12
1979	22.36	21.67	22.07	21.27	4.70	12.50	6.63	8.04	16.86	8.56	15.07
1980	10.89	(10.31)	1.08	(0.18)	(9.53)	(4.64)	(7.63)	(13.16)	17.42	11.75	(0.39)
1981	43.19	39.60	41.45	34.80	14.99	9.45	12.51	20.38	14.71	15.76	26.60
1982	(17.88)	(19.64)	(18.77)	(15.00)	11.08	0.40	6.20	(0.69)	17.51	17.95	(7.85)
1983	40.91	23.60	33.55	31.60	32.53	14.54	24.89	20.54	7.07	12.76	27.05
1984	5.08	32.46	15.66	17.30	5.46	12.42	8.67	8.20	13.33	13.07	13.01
1985	20.75	(6.82)	9.54	7.20	17.86	(8.22)	4.53	5.50	13.47	3.62	8.09
1986	34.95	58.48	43.44	56.02	54.30	50.33	51.21	48.70	10.75	6.95	41.52
1987	21.63	43.88	30.01	43.22	9.14	32.63	22.59	17.42	12.67	11.97	24.69
1988	(12.18)	2.15	(4.74)	5.81	3.26	20.24	12.65	11.42	9.19	7.67	3.10
1989	13.20	10.00	11.30	13.56	2.10	(5.50)	(2.40)	0.36	8.20	10.40	5.90

Year	Equities				Bonds				Real estate	Short term	Total Fund
	United States	Outside United States	Total	MSCI World Index[a]	United States	Outside United States	Total[b]	CWG Bond Index[c]			
1990	21.54	13.21	16.57	(2.30)	10.47	2.93	6.20	3.12	12.31	9.72	11.56
1991	8.9	1.2	4.5	3.2	12.5	17.4	15.0	16.2	5.1	13.1	8.9
1992	11.3	0.1	4.9	(0.5)	13.7	14.0	14.0	14.0	(4.1)	6.5	7.6
1993	17.3	6.7	11.2	12.7	15.9	17.7	16.9	19.0	(6.6)	7.5	11.6
1994	(2.7)	24.4	12.4	14.0	3.4	10.1	7.7	6.8	0.5	3.0	9.7
1995	11.1	6.5	8.1	9.8	2.9	18.6	12.9	12.1	0.0	5.0	8.7
1996	30.2	15.1	20.5	20.6	8.0	3.3	5.1	5.3	10.4	4.1	14.6
1997	18.9	7.2	11.6	9.8	6.2	2.5	3.6	1.2	8.6	4.4	8.9
1998	45.4	15.4	27.3	32.4	10.6	4.3	7.0	5.4	18.9	7.0	20.4
1999	18.4	9.7	13.9	13.0	4.8	9.0	6.5	10.0	4.8	9.9	11.3
2000	17.5	39.9	28.5	21.6	3.1	(5.7)	(2.5)	(0.3)	11.7	3.0	18.0
2001	(17.2)	(30.3)	(24.2)	(25.1)	13.0	(4.2)	2.0	(1.7)	11.3	4.2	(15.0)
2002	2.8	(6.1)	(1.3)	(4.2)	4.9	2.1	3.1	0.5	8.4	3.5	0.7
2003	(23.9)	(21.7)	(23.1)	(24.2)	15.9	34.9	28.4	25.2	8.5	11.1	-3.8
2004	29.3	56.5	42.5	43.9	6.8	19.4	15.7	13.5	23.9	8.1	28.7
2005	6.3	16.9	11.8	11.1	1.2	10.5	7.8	5.5	15.8	2.5	10.4
2006	13.1	28.8	21.3	18.6	2.4	-4.4	-2.8	-2.0	30.5	2.9	13.3
2006				20.3 MSCIAC[d]				-2.6 BCGA[e]			12.3[f] 60/31
2007	9.4	20.6	15.7	16.4 MSCIAC[d]	7.1	9.4	8.4	8.1 BCGA[e]	24.0	5.5	13.4[f] 60/31
2008	-0.6	5.9	3.4	-0.7 MSCIAC[d]	8.3	18.4	15.1	15.3 BCGA[e]	9.0	8.3	8.1[f] 60/31
2009	-34.6	-45.1	-41.0	-42.7 MSCIAC[d]	-1.4	-12.6	-8.6	-4.9 BCGA[e]	-22.9	3.9	-28.3[f] 60/31
2010	42.6	62.2	54.1	56.3 MSCIAC[d]	5.9	16.7	10.8	10.2 BCGA[e]	-17.4	-2.7	32.2

[a] The MSCI World Index consists of 23 major equity markets.
[b] The proportion of bonds held outside the United States was not significant prior to 1975.
[c] The Solomon Brothers World Government Bond Index is now the Citigroup World Government Bond Index, which consists of 18 major bond markets.
[d] The MSCI All Country World Index consists of 23 developed and 23 emerging markets.
[e] Barclays Capital Global Aggregate Bond Index (name change from Lehman Brothers Global Aggregate Index, effective 3 November 2008).
[f] The Strategic Asset Allocation 60/31 policy benchmark is comprised of the following components: 60 per cent MSCI All Country World Index, 31 per cent Barclays Capital Global Aggregate Bond Index, 6 per cent National Council of Real Estate Investment Fiduciaries Open-End Diversified Core Equity Index and 3 per cent Merrill Lynch 91-day Treasury bill.

Table 5
Fund annual rates of return based on market value
(Percentages for selected periods ending 31 March 2010)

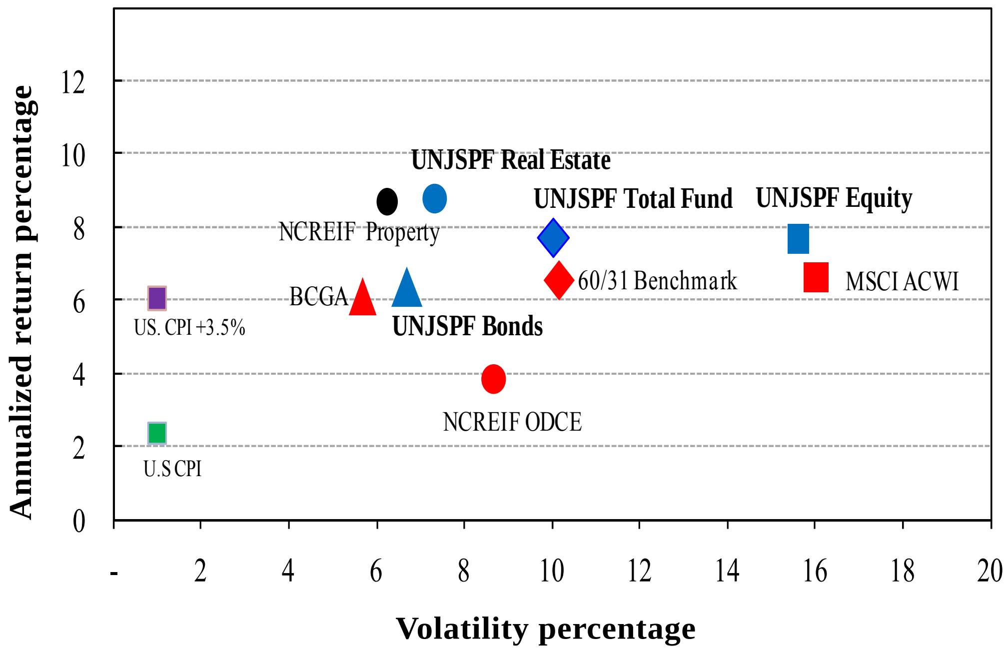
	2010	*2009*	*2008*	*5 years to 2010*	*10 years to 2010*	*15 years to 2010*
United States equities	42.6	-34.6	-0.6			
Equities outside United States	62.2	-45.1	3.9			
Total equities	**54.1**	**-41.0**	**3.4**	**5.7**	**1.9**	**7.7**
United States bonds	5.9	-1.4	8.3			
Bonds outside United States	16.7	-12.6	18.4			
Total bonds	**10.8**	**-8.6**	**15.1**	**4.2**	**7.6**	**6.4**
Real estate-related	-17.4	-22.9	9.0	2.4	7.8	8.8
Short-term investments	-2.7	3.9	8.3	3.5	4.8	—
Total Fund in United States dollars	**32.2**	**-28.3**	**8.1**	**5.7**	**4.4**	**7.7**
Inflation-adjusted return (based on United States CPI)	**29.2**	**-28.1**	**4.0**	**3.2**	**1.9**	**4.7**

D. Risk-return profile

63. Over the past 15 years, the Fund's average annual return of 7.7 per cent was higher than the benchmark's return of 6.6 per cent. The Fund's volatility of 10.0 per cent was slightly lower than the benchmark's 10.2 per cent volatility. The Fund had a better risk-return profile because it has a well-diversified portfolio that includes all major asset classes and securities.

64. Within asset classes, the Fund's equity portfolio return of 7.7 outperformed the MSCI All Country World Index return of 6.6, but the Fund's equity portfolio had a much better risk profile (15.6 per cent) compared with the MSCI All Country World Index (16.03 per cent). The bond portfolio (with a 15-year average return of 6.4 per cent) outperformed the Barclays Capital Global Aggregate Bond Index (6.1 per cent) but had higher volatility (6.7 per cent) compared with that Index (5.7 per cent).

Figure III
Fund 15-year risk-return profile vs. indices through 31 March 2010



VI. Investments in developing countries

65. The Fund continues to make efforts to invest in developing countries to the extent that this has been consistent with the interests of participants and beneficiaries. Direct and indirect investments in developing countries amounted to $4.8 billion on 31 March 2010, an increase of approximately 25 per cent from $3.8 billion at cost on 31 March 2008. The increases were in the developing Asia region and the Latin America region.

66. The Investment Management Division continues to explore possible investment opportunities in developing countries. Investment visits were undertaken in Africa, Asia, Latin America and Eastern Europe during the period under review. The Fund continues to review its exposure in these markets in search of suitable investment instruments while taking into account the overall investment criteria and strategy of the Fund. It also continues to explore opportunities in sovereign debt for which credit quality has improved.

Table 6
Development-related investment: book value as at 31 March 2008 and 31 March 2010
(in thousands of United States dollars)

	Book value		*Market value*		
Region	*Total 2008*	*Total 2010*	*Total 2008*	*Total 2010*	*Two-year annualized return (percentage)*
Africa					
Egypt	24 609	14 799	22 998	17 226	n/a[a]
South Africa	331 946	242 903	310 697	350 483	n/a[a]
Regional funds	91 198	110 044	221 651	121 707	(10.52)
Subtotal	**447 753**	**367 746**	**555 346**	**489 416**	**n/a[a]**
Development institutions	59 348	79 203	69 628	85 912	
Total Africa	**507 101**	**446 949**	**624 974**	**575 328**	
Asia					
China	376 087	872 935	248 197	1 140 989	n/a[a]
India	115 115	180 663	231 161	302 472	(5.15)
Malaysia	606 909	513 681	661 941	562 907	3.95
Qatar	28 626	10 002	29 737	10 462	n/a[a]
Republic of Korea	637 088	653 007	674 235	795 906	1.54
Singapore	625 499	180 568	747 995	253 741	21.77
Regional funds	3 804	261 624	339 504	216 141	n/a[a]
Subtotal	**2 393 128**	**2 672 480**	**2 932 770**	**3 282 618**	
Development institutions	83 103	55 118	86 693	58 739	
Total Asia	**2 476 231**	**2 727 598**	**3 019 463**	**3 341 357**	
Europe					
Cyprus	26 229	0	50 214	0	n/a[a]
Turkey	61 176	73 312	73 475	110 793	13.03
Regional funds	0	0	0	0	n/a[a]
Subtotal	**87 405**	**73 312**	**123 689**	**110 793**	
Development institutions	0	0	0	0	
Total Europe	**87 405**	**73 312**	**123 689**	**110 793**	
Latin America					
Argentina	6 720	0	8 886	0	n/a[a]
Brazil	95 951	276 823	327 669	571 686	7.20
Chile	37 846	20 056	36 972	45 499	11.06
Colombia	0	2 951		4 830	n/a[a]
Mexico	448 786	444 034	595 490	593 348	5.82

Region	Book value Total 2008	Book value Total 2010	Market value Total 2008	Market value Total 2010	Two-year annualized return (percentage)
Venezuela (Bolivarian Republic of)	0	19 965	0	24 023	n/a[a]
Regional funds	0	0	0	0	
Subtotal	**589 303**	**763 829**	**969 017**	**1 239 386**	
Development institutions	30 564	136 316	31 476	141 999	
Total Latin America	**619 867**	**900 145**	**1 000 493**	**1 381 385**	
Other development funds					
International Bank for Reconstruction and Development	101 338	318 025	163 342	351 964	n/a[a]
European Investment Bank		315 002		323 446	n/a[a]
Fiduciary Emerging Market Bond Fund	21 600	21 600	37 541	36 951	(0.79)
Emerging Market Middle East Fund	17 265	19 746	26 659	15 793	(23.03)
Emerging Market Investors Fund	30 501	0	93 049	0	n/a[a]
Total other development funds	**170 704**	**674 373**	**320 591**	**728 154**	
Grand total	**3 861 308**	**4 822 377**	**5 089 210**	**6 137 017**	

[a] n/a denotes cases in which the securities are not held at the beginning/ending period in a custom region and the returns are not available from the independent master record-keeper.

VII. Conclusion

67. The Fund has performed steadily, in excess of its benchmarks, during the unprecedented volatility of the past year. During this time, several initiatives have been undertaken to strengthen the investment decisions and the supporting infrastructure. To build a sounder investment process, the Investment Management Division has implemented an ongoing system for documenting the initial logic behind each investment, requiring the monitoring of key risk factors. The implementation of the trade order management system, completed in the first half of 2010, provides straight-through processing of equity trades and a clear audit trail, and documents pre-trade compliance. Additional compliance and financial disclosure rules have been inaugurated to ensure that staff of the Investment Management Division observe the highest standards of ethical conduct. Despite the choppy and trendless markets that the Fund may be facing during this phase of the global economic recovery, with the support of the additional staff and investment tools added during the biennium, the Investment Management Division will be in a position to safeguard the Fund and build a stronger foundation for the future.