Havering
LONDON BOROUGH

PENSIONS COMMITTEE
14 June 2016

Subject Heading:	**PENSION FUND PERFORMANCE MONITORING FOR THE QUARTER ENDED MARCH 2016**
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Policy context:	Pension Fund Managers' performances are regularly monitored in order to ensure that the investment objectives are being met.
Financial summary:	This report comments upon the performance of the Fund for the period ended 31 March 2016

The subject matter of this report deals with the following Council Objectives

Havering will be clean and its environment will be cared for	[]
People will be safe, in their homes and in the community	[]
Residents will be proud to live in Havering	[x]

SUMMARY

This report provides the Committee with an overview of the performance of the Havering Pension Fund investments for the quarterly period to 31 March 2016. The performance information is taken from the Quarterly Performance Report supplied by each Investment Manager, the WM Company Quarterly Performance Review Report and Hymans Monitoring Report.

The net return on the Fund's investments for the **quarter** to 31 March 2016 was **1.4%.** This represents an under performance of -**0.8%** against the tactical benchmark and an under performance of -**6.9%** against the strategic benchmark.

The overall net return of the Fund's investments for the **year** to 31 March 2016 was **-1.2%.** This represents under performance of **-2.8%** against the tactical combined benchmark and under performance of **-7.7%** against the annual strategic benchmark. The annual strategic benchmark is a measure of the fund's performance against a target based upon gilts + 1.8% (the rate which is used in the valuation of the funds liabilities). The implications of this shortfall are discussed further in paragraphs 1.2 and 1.3 below.

It is now possible to measure the individual managers' annual return for the new tactical combined benchmark since they became active on the 14th February 2005. These results are shown later in the report.

RECOMMENDATIONS

That the Committee:

1) Considers Hymans performance monitoring report and presentation (Appendix A).
2) Receive a presentation from the Fund's Multi-Asset Manager (GMO Global Real Return).
3) Notes the summary of the performance of the Pension Fund within this report.
4) Considers the quarterly reports provided by each investment manager.
5) Considers and notes any Corporate Governance issues arising from voting as detailed by each manager.
6) Considers any points arising from officer monitoring meetings (section 4 refers).
7) Notes the analysis of the cash balances (paragraphs 2.2 and 2.3 refers).

REPORT DETAIL

1. Background

1.1 The Fund undertook a full review of the Statement of Investment Principles (SIP) during 2012/13 and following the appointments of the Multi Asset Managers this almost completes the fund's restructuring. The Fund is still considering options for an investment in Local Infrastructure.

1.2 A strategic benchmark has been adopted for the overall Fund of Gilts + 1.8% (net of fees) per annum. This is the expected return in excess of the fund's liabilities over the longer term. The strategic benchmark measures the extent to which the fund is meeting its longer term objective of reducing the funds deficit. This current shortfall is driven by the historically low level of interest rates which drive up the value of gilts (and consequently the level of the fund liabilities). Whether interest rates will remain at those levels for the longer term and the implications for the Fund's Investment strategy is a matter which will need to be considered at the time of the next actuarial review.

1.3 Our Investment Advisors have stated that there are things that could have been done to protect the fund against falling interest rates (e.g. hedging) but they do not believe that this action would have been appropriate. The Fund is already partially protected through its investments with Royal London and given the long term nature of the fund they believe that the fund objective of pursuing a stable investment return remains appropriate. They also note that although the value placed on the liabilities has risen as a result of falling yields, inflation and expectations of future inflation has fallen meaning that the actual benefit cash flows expected to be paid from the fund will be lower.

1.4 Individual manager performance and asset allocation will determine the out performance against the strategic benchmark. Each manager has been set a specific (tactical) benchmark as well as an outperformance target against which their performance will be measured. This benchmark is determined according to the type of investments being managed. This is not directly comparable to the strategic benchmark as the majority of the mandate benchmarks are different but contributes to the overall performance.

1.5 The following table reflects the asset allocation split :

Asset Class	Target allocation	Investment Manager/ product	Segregated /pooled	Active/ Passive	Benchmark and Target
UK/Global Equity	12.5%	Baillie Gifford (Global Alpha Fund)	Pooled	Active	MSCI All Countries Index plus 2.5%
	6.25%	State Street Global Asset	Pooled	Passive	FTSE All World Equity Index
	6.25%	State Street Global Asset	Pooled	Passive	FTSE RAFI All World 3000 Index
Multi Asset Strategy	15%	Baillie Gifford (Diversified Growth Fund)	Pooled	Active	UK Base Rate plus 3.5%
	20%	GMO Global Real return (UCITS)	Pooled	Active	OECD CPI g7 plus 3 - 5%
Absolute	15%	Ruffer	Segregated	Active	LIBOR+

Asset Class	Target allocation	Investment Manager/ product	Segregated /pooled	Active/ Passive	Benchmark and Target
Return					
Property	5%	UBS	Pooled	Active	IPD All balanced (property) Fund's median +
Gilt/Investment Bonds	17%	Royal London	Segregated	Active	• 50% iBoxx £ non- Gilt over 10 years • 16.7% FTSE Actuaries UK gilt over 15 years • 33.3% FTSE Actuaries Index-linked over 5 years. Plus 1.25%*
Infrastructure	3%	State Street Global Assets –Sterling liquidity Fund Cash is invested pending identification of a local infrastructure project.			

*0.75% prior to 1 November 2015

1.6 UBS, SSgA, GMO and Baillie Gifford manage the assets on a pooled basis. Royal London and Ruffer manage the assets on a segregated basis. Performance is monitored by reference to the benchmark and out performance target. Each manager's individual performance is shown in this report with a summary of any key information relevant to their performance.

1.7 Since 2006, to ensure consistency with reports received from our Performance Measurers, Investments Advisors and Fund Managers, the 'relative returns' (under/over performance) calculations has been changed from the previously used arithmetical method to the industry standard geometric method (please note that this will sometimes produce figures that arithmetically do not add up).

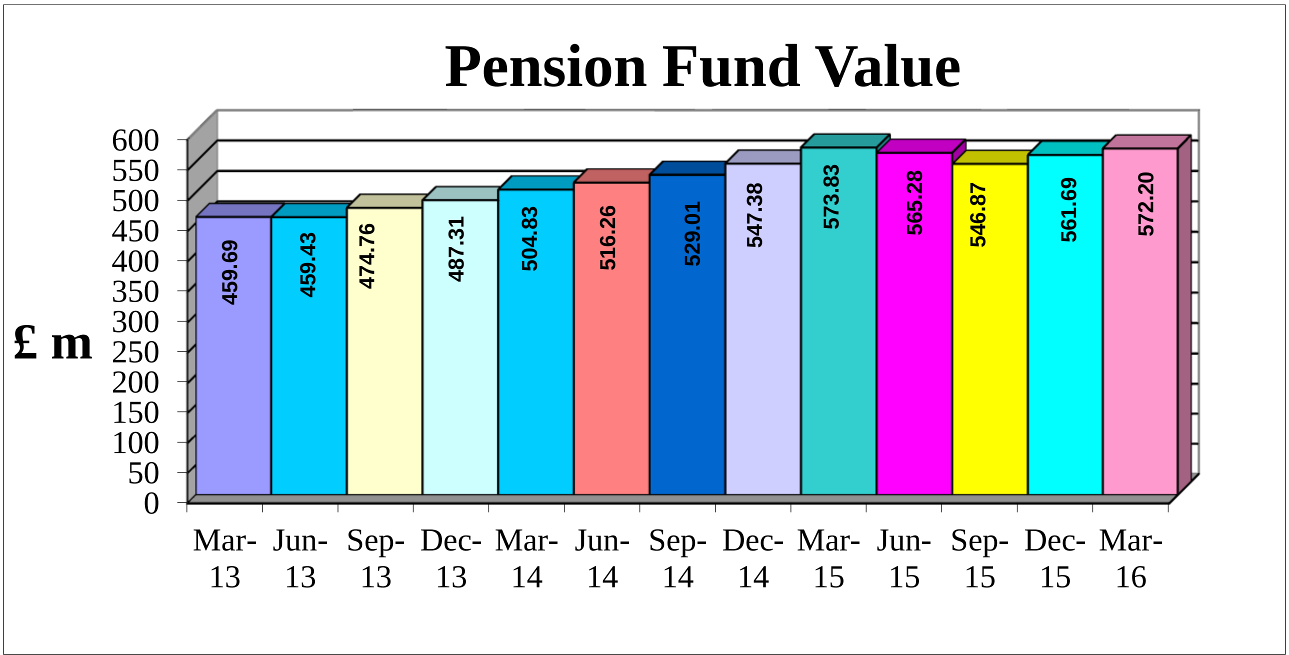
1.8 Existing Managers are invited to present at the Pensions Committee Meeting every six months. On alternate dates, they meet with officers for a formal monitoring meeting. The exception to this procedure are the pooled Managers (SSgA, UBS, Baillie Gifford and GMO) and Ruffer who will attend two meetings per year, one with Officers and one with the Pensions Committee. However if there are any specific matters of concern to the Committee relating to the

Managers performance, arrangements will be made for additional presentations.

1.9 Hyman's performance monitoring report is attached at **Appendix A.**

2. Fund Size

2.1 Based on information supplied by our performance measurers the total combined fund value at the close of business on 31 March 16 was **£572.20m**. This valuation differs from the basis of valuation used by our Fund Managers and our Investment Advisor in that it excludes accrued income. This compares with a fund value of £561.69m at the 31 December 15; an **increase** of **£10.52m**. The movement in the fund value is attributable to an increase in assets of £8.53m and an increase in cash of £1.99m. The internally managed cash level stands at **£11.65m** of which an analysis follows in this report.



Source: WM Company (Performance Measurers)

2.2 An analysis of the internally managed cash balance of **£11.65m** follows:

CASH ANALYSIS	**2013/14 31 Mar 15**	**2014/15 31 Mar 15 Updated**	**2015/16 31 Mar 16**
	£000's	£000's	£000's
Balance B/F	**-3474**	**-5661**	**-7599**
Benefits Paid	32552	33568	35048
Management costs	2312	1600	1735
Net Transfer Values	-1131	-135	1018
Employee/Employer Contributions	-45659	-35306	-42093
Cash from/to Managers/Other Adj.	9825	-1618	306

Internal Interest	-86	-47	-67
Movement in Year	**-2187**	**-1938**	**-4053**
Balance C/F	**-5661**	**-7599**	**-11652**

2.3 Members agreed the updated cash management policy at its meeting on the 15 December 2015. The policy sets out that should the cash level fall below the de-minimus amount of £3m this should be topped up to £6m. This policy includes drawing down income from the bond and property manager when required.

2.4 The cash management policy also incorporates a threshold for the maximum amount of cash that the fund should hold and introduced a discretion that allows the Chief Executive to exceed the threshold to meet unforeseeable volatile unpredictable payments.

3. Performance Figures against Benchmarks

3.1.1 The overall net performance of the Fund against the new **Combined Tactical Benchmark** (the combination of each of the individual manager benchmarks) follows:

	Quarter to 31.03.16	**12 Months to 31.03.16**	**3 Years to 31.03.16**	**5 years to 31.03.16**
Fund	1.4%	-1.2%	6.1%	7.3%
Benchmark	2.2%	1.7%	5.9%	7.0%
*Difference in return	-0.8%	-2.8%	0.3%	0.4%

Source: WM Company

**Totals may not sum due to geometric basis of calculation and rounding.*

3.1.2 The overall net performance of the Fund against the **Strategic Benchmark** (i.e. the strategy adopted of Gilts over 15 years + 1.8% Net of fees) is shown below:

	Quarter to 31.03.16	**12 Months to 31.03.16**	**3 Years to 31.03.16**	**5 years to 31.03.16**
Fund	1.4%	-1.2%	6.1%	7.3%
Benchmark	8.9%	7.1%	11.6%	14.2%
*Difference in return	-6.9%	-7.7%	-4.9%	-6.0%

Source: WM Company

**Totals may not sum due to geometric basis of calculation and rounding.*

3.1.3 The following tables compare each manager's performance against their **specific (tactical) benchmark** and their **performance target** (benchmark plus the agreed mandated out performance target) for the current quarter and the last 12 months.

QUARTERLY PERFORMANCE (AS AT 31 MARCH 2016)

Fund Manager	Return (Performance)	Benchmark	Performance vs benchmark	Target	Performance vs Target
Royal London	5.10	5.82	**-0.72**	6.01	**-0.91**
UBS	1.43	1.38	**0.05**	n/a	**n/a**
Ruffer	-0.03	0.10	**-0.13**	n/a	**n/a**
SSgA Global Equity	2.93	2.94	**-0.01**	n/a	**n/a**
SSgA Fundamental Index	3.16	3.14	**0.02**	n/a	**n/a**
SSgA Sterling Liquidity Fund	0.14	0.09	**0.05**	n/a	**n/a**
Baillie Gifford (Global Alpha Fund)	0.40	2.90	**-2.50**	3.53	**-3.13**
London CIV/Baillie Gifford (DGF)	-0.1	1.00	**-1.1**	n/a	**n/a**
GMO	-0.03	-0.02	**-0.01**	n/a	**n/a**

Source: WM Company, Fund Managers and Hymans

- Totals may not sum due to geometric basis of calculation and rounding.

ANNUAL PERFORMANCE (LAST 12 MONTHS)

Fund Manager	Return (Performance)	Benchmark	Performance vs benchmark	Target	Performance vs Target
Royal London	1.42	1.02	**0.40**	1.77	**-0.35**
UBS	11.63	11.24	**0.39**	n/a	**n/a**
Ruffer	-3.47	0.60	**-4.07**	n/a	**n/a**
SSgA Global Equity	0.53	0.56	**-0.03**	n/a	**n/a**
SSgA Sterling Liquidity Fund	0.53	0.36	**0.17**	n/a	**n/a**
Baillie Gifford (Global Alpha Fund)	0.10	-0.60	**0.70**	1.90	**-1.80**
London CIV/Baillie Gifford (DGF)	-1.40	4.00	**-5.20**	n/a	**n/a**
GMO	-5.58	0.14	**-5.72**	n/a	**n/a**

Source: WM Company, Fund Managers and Hymans

- Totals may not sum due to geometric basis of calculation and rounding.
- SSgA fundamental Index not invested for entire period

Pensions Committee, 14 June 2016

4. Fund Manager Reports

4.1. UK Investment Grade Bonds (Bonds Gilts, UK Corporates, UK Index Linked, UK Other) – (Royal London Asset Management)

a) In accordance with agreed procedures officers met with representatives from Royal London on the 11 May 2016 at which a review of their performance as at 31 March 16 was discussed.

b) The fund achieved a net return of 5.10% during the quarter and under-performed the benchmark for the quarter by -0.72%. Royal London outperformed the benchmark over the one year period by 0.40%. Since inception they outperformed the benchmark by 0.57%.

c) With effect from the 1 November 2015 the return objective was increased from 0.75% to 1.25% and following a change to the mandate's performance target and permissible investments, an exposure totalling 8.2% of Fund assets was established in the Royal London Sterling Extra Yield Bond Fund.

d) Asset Allocation within the portfolio was 52.6% Conventional credit bonds, 29.1% Index linked sovereign bonds, 9.6% Sterling conventional gilts, 7.6% RL Sterling extra yield bond fund, 0.1% Overseas conventional credit bonds and 0.9% in cash.

e) There has only been small portfolio changes during the quarter, an increase allocations in index linked sovereign bonds, funded by the sale of Sterling conventional gilts and conventional credit bonds. The portfolio remains overweight in Conventional credit bonds remaining underweight in Sterling conventional gilts and Index linked sovereign bonds.

f) Royal London reported on market events during the quarter:

- Government bonds (Gilts) returned 4.92% over the quarter. Yields fell sharply across maturities, medium dated gilts outperformed, with long dated gilts impacted by heavy demand. Both European and Japanese government bonds outperformed gilts. The ECB cut deposit rates further and extended it QE programme, with the Japanese banks following the ECB in cutting interest rates below zero.

- Index linked gilts returned 5.67% over the quarter, real yields fell across all maturities, and initial concerns over global growth drove yield moves. A further slump in oil prices early in the quarter led to the re-emergence of deflation concerns and a fall in demand for inflation linked securities. Royal London's relative preference for index-linked bonds was marginally increased over the quarter that was a small benefit for overall fund performance. UK index linked gilts were expensive compared to overseas and off benchmark positions in US, Australian, French and German index linked bonds were actively traded through the quarter, which added to performance.

- Sterling credit bonds returned 3.01% over the quarter. Corporate bonds in non-financials out performed financials, which was the reverse of last year's performance. Sterling bond issuance remain subdued as concerns over China and the outlook for global growth added to the already tepid liquidity conditions, with many sterling issuers waiting until after the June EU referendum.

h) The relative fund performance over the quarter was principally a result of asset allocation, duration and yield curve positioning. The main positive and negative contributors to performance during the quarter are as follows:

- Royal London maintained their underweight exposure to government bonds in favour of corporate bonds this quarter, concerns for the outlook for global growth re-emerged, the start of 2016 was characterised by a volatile financial market and a sharp fall in government bond yields, although managed to recover by the end of the quarter. This asset allocation detracted from fund performance.

- Off benchmark exposure to shorter dated credit bonds and overweight exposure to ultra long dated index linked government bonds negatively impacted performance.

- Royal London's overweight position in financial bonds and underweight exposure to supranational debt and the industrial sector was not beneficial to performance

- Tactical trading in gilts and index- linked gilts had a positive impact on performance.

i) Royal London believes that UK base rates will rise by the end of 2016 and have held a short duration position. We asked them what their drivers for this view are given that the markets do not now imply a rate rise for next 2-3 years. They said they believe the current global economic expansion will sustain through 2016, they also expect oil prices to rise by the end of 2016 to more normal levels (oil prices have fallen by approximately 80%) which will increase inflation and is the first step to an interest rate rise. If interest rates remain lower for longer than they expect they do not think this will not have an adverse effect on the portfolio as they have a positive well maintained position, again noting that credit companies do well when interest rates are low.

j) We asked Royal London, to what extent do they believe ESG considerations are relevant to bond investment and how do they integrate ESG issues in their credit research and management of bond portfolio (ESG - environmental, social and governance refers to the three central factors in measuring the sustainability and ethical impact of an investment in a company or business). They said that they did not have any ESG screens and they do not consider ESG issues for this fund. However, market forces indirectly impact ESG implications on the portfolio, by making investments more or less attractive. For instance climate change could have an impact water companies, investment in Water Boards could be more attractive in North Yorkshire than down in the south of England due to rain fall levels.

k) No governance or whistle blowing issues was reported.

4.2. Property (UBS)

a) In accordance with agreed procedures officers will only meet with representatives from UBS once in the year with the other meeting to be held with members. Representative from UBS last met with Officers on the 20 August 2015 at which a review of their performance as at 30 June 15 was discussed. UBS last met with members of the Pension Committee on the 15 March 2016 at which they covered the period ending up to 31 December 2015.

b) UBS delivered a return of 1.43% over the quarter, outperforming the benchmark by 0.05%. The Fund is ahead of the benchmark over the year by 0.39%.

c) Following the Pensions Committee decision on the 15 December 2015 £5.5m was withdrawn from the SSgA Sterling Liquidity Fund on the 3 February 2016 to purchase additional units in the UBS Triton Fund.

4.3. Multi Asset Manager (Ruffer)

a) In accordance with agreed procedures officers will only meet with representatives from Ruffer once in the year with the other meeting to be held with members. The Pensions Committee last met with Ruffer at the 22 September 2015 meeting at which their performance as at the end of June 15 was discussed. Officers last met with representatives from Ruffer on 05 February 2015 at which a review of their performance as at 31 December 2015 was discussed.

b) Since Ruffer last met with officers, to discuss the December 15 quarter end, there has been no change in the value of the fund.

c) Ruffer delivered a return of -0.03% (net of fees) over the quarter, underperforming the benchmark by -0.13%. Over the last 12 months Ruffer delivered a return of -3.47% underperforming the benchmark by -4.07%.

d) Representatives from Ruffer and officers are preparing to transfer assets into the London CIV. It is anticipated that this will take place during the latter half of June 2016.

e) No whistle blowing issues or governance was reported.

4.4. Passive Equities Manager (SSgA)

a) In accordance with agreed procedures officers will only meet with representatives from SSgA once in the year with the other meeting to be held with members. SSgA last met with the members of the Pension Committee on the 15 December 2015 at which they covered the period ending up to 31 September 2015. Officers met with representatives from SSgA on the 11 May 2016 at which a review of their performance as at 31 March 16 was discussed.

b) Value of the fund has decreased since members last met with SSGA by 4.09%

c) The new SSgA Fundamental Index commenced on the 20 August 2015.

d) The SSgA mandate is now split into three components, Sterling Liquidity sub fund, SSgA All World Equity Index sub fund, and the Fundamental Index Global Equity sub fund.

e) SSGA has performed in line with the benchmark over the latest quarter, as anticipated from an index-tracking mandate

f) We asked SSGA how they approached corporate engagement and voting within its managed index tracking equity portfolios and to what extent do they believe that active engagement conflicts with the concept of passive management. They said that their proxy voting and engagement strategy is designed to meet the needs of UK clients; they have a standard proxy voting policy that they only deviate from on rare occasions that are justified by special circumstances specific to an individual company. SSGA vote with the aim of ensuring that clients receive the best possible returns on their investment and company policies are in the best interest of their shareholders. They do not want to interfere with the day to day operations of the companies, but want to make sure the management are effective and wanting to maximise the shareholder return.

g) Following the Pensions Committee meeting on the 15 December 2015 and a further decision to purchase additional units in the UBS Triton Property Fund, £5.5m was withdrawn from the SSgA Sterling Liquidity Fund on the 3 February 2016.This is reflected in the decrease of value of the SSgA portfolio.

h) No governance issues or whistle blowing was reported.

4.5. Global Equities Manager (Baillie Gifford)

a) In accordance with agreed procedures officers met with representatives from Baillie Gifford on the 4 February 2016 at which a review of their performance as at 31 December 15 was discussed.

b) The value of the fund increased by 0.36% over the last quarter.

c) The Global Alpha Fund delivered a return of 0.40% (net of fees) over the quarter, underperforming the benchmark by -2.50%. Over the last 12 months Baillie Gifford delivered a return of 0.10% outperforming the benchmark by 0.70%.

d) This mandate transferred to the London CIV on the 11 April 2016.

e) No governance or whistle blowing issues were reported

4.6. Multi Asset Manager (Baillie Gifford Diversified Growth Fund)

a) In accordance with agreed procedures officers met with representatives from Baillie Gifford on the 4 February 2016 at which a review of their performance as at 31 December 15 was discussed.

b) This mandate was transferred to the London CIV on the 15 February 2016.

c) The London CIV will oversee the monitoring and review of the performance of this mandate and we will expect some feedback from the London CIV in due course.

4.7. Multi Asset Manager (GMO – Global Real Return (UCITS) Fund)

a) In accordance with agreed procedures officers will only meet with representatives from GMO once in the year with the other meeting to be held with members. GMO last met with the members of the Pension Committee on the 23 June 2015 at which they covered the period ending up to 31 March 2015. Officers met with representatives from GMO on the 5 November 2015, at which a review of their performance as at 30 September 15 was discussed.

b) Representatives from GMO are due to make a presentation at this Committee therefore a brief overview of their performance as at 31 March 2016 follows.

c) The fund achieved a net return of 0.03% during the quarter and underperformed the benchmark for the quarter by -0.01%. Over the last 12 months GMO delivered a return of -5.58% underperforming the benchmark by -5.72%.

d) The GMO investment is in a dynamic multi-asset fund, the GMO Global Real Returns UCITS Fund (GRRUF) and targets a return of CPI+5% (net of fees) over a full 7 year cycle. The Fund invests globally in equities, debt, money market instruments, currencies, instruments relating to commodities indices, REITS and related derivatives.

e) GMO philosophy is to buy undervalued assets with a long term view to assets returning to fair value.

f) The asset allocation within the portfolio was 43% Equities, 15% Alternative strategies, 22% Fixed Income and 20% Cash/Cash Plus.

5. Corporate Governance Issues

The Committee, previously, agreed that it would:

1. Receive quarterly information from each relevant Investment Manager, detailing the voting history of the Investment Managers on contentious issues. This information is included in the Managers' Quarterly Reports, which will be distributed to members electronically.

2. Receive quarterly information from the Investment Managers, detailing new Investments made.

   - Points 1 and 2 are contained in the Managers' reports.

3. Voting – Where the fund does not hold a pooled equity holding, Members should select a sample of the votes cast from the voting list supplied by the managers (currently only Ruffer) which is included within the quarterly report and question the Fund Managers regarding how Corporate Governance issues were considered in arriving at these decisions.

This report is being presented in order that:

- The general position of the Fund is considered plus other matters including any general issues as advised by Hymans.

- Hymans will discuss the managers' performance after which the particular manager will be invited to join the meeting and make their presentation. The managers attending the meeting will be from:

GMO

- Hymans and Officers will discuss with Members any issues arising from the monitoring of the other managers.

IMPLICATIONS AND RISKS

Financial implications and risks:

Pension Fund Managers' performances are regularly monitored in order to ensure that the investment objectives are being met and consequently minimise any cost to the General Fund

Legal implications and risks:

None arising directly

Human Resources implications and risks:

There are no immediate HR implications. However longer term, shortfalls may need to be addressed depending upon performance of the fund.

Equalities implications and risks:

None arising that directly impacts on residents or staff.

BACKGROUND PAPERS

Royal London Quarterly report to 31 March 2016
UBS Quarterly report to 31 March 2016
Ruffer Quarterly report 31 March 2016
State Street Global Assets report to 31 March 2016
Baillie Gifford Quarterly Reports 31 March 2016
GMO Quarterly Report 31 March 2016
The WM Company Performance Review Report to 31 March 2016