



PENSIONS COMMITTEE 24 September 2013	REPORT

Subject Heading:	PENSION FUND PERFORMANCE MONITORING FOR THE QUARTER ENDED 30 JUNE 2013
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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 30 June 2013

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

Clean, safe and green borough	<input type="checkbox"/>
Excellence in education and learning	<input type="checkbox"/>
Opportunities for all through economic, social and cultural activity	<input type="checkbox"/>
Value and enhance the life of every individual	<input checked="" type="checkbox"/>
High customer satisfaction and a stable council tax	<input type="checkbox"/>

SUMMARY

This report provides the Committee with an overview of the performance of the Havering Pension Fund investments for the quarterly period to 30 June 2013. 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 30 June 2013 was **-0.4%**. This represents an out performance of **1.0%** against the combined tactical benchmark and an out performance of **5.0%** against the strategic benchmark.

The overall net return of the Fund's investments for the **year** to 30 June 2013 was **16.6%**. This represents an out performance of **3.3%** against the annual tactical combined benchmark and an out performance of **18.7%** against the annual strategic benchmark.

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 - exempt).
- 2) Receive a presentation from the Funds UK Equities Manager (Standard Life) and the Funds Investment Grade Bonds Manager (Royal London).- exempt
- 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 whilst this was on-going members agreed an interim change to the strategy in December 2012 which increased the asset

Pensions Committee, 24 September 2013

allocation to the Absolute Return Manager from 10% to 15%. The final SIP was agreed in March 2013 and the portfolio is currently being restructured to reflect those decisions.

- 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 main factor in meeting the strategic benchmark is market performance.**
- 1.3 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.
- 1.4 Changes to the Asset Allocation targets were agreed by members at the Pensions Committee meeting on the 26 March 2013. The long term strategy of the fund adopted at the meeting is to reduce exposure to equities and invest in multi asset strategies. Pending appointment of the providers of the multi-asset mandates members agreed to adopt an interim strategy which considered the fund rebalancing its overweight position in equities. During May, 5% of the fund was switched from SSgA's UK/Global Equities Manager to an SSgA cash fund. The long term strategy decisions are likely to be progressed during September 2013. No other changes have yet been made to the individual manager allocation and are shown in the following table against the manager's benchmarks:

Manager and % of target fund allocation	Mandate	Tactical Benchmark	Out performance Target
Standard Life 17%	UK Equities - Active	FTSE All Share Index	2%
State Street (SSgA) 21%	UK/Global Equities - passive	UK- FTSE All Share Index Global (Ex UK) – FTSE All World ex UK Index	To track the benchmark
Baillie Gifford Street 17%	Global Equities - Active	MSCI AC World Index	1.5 – 2.5% over rolling 5 year period
Royal London Asset Management 20%	Investment Grade Bonds	<ul style="list-style-type: none"> • 50% iBoxx Sterling Non Gilt Over 10 Year Index • 16.7% FTSE Actuaries UK • Gilt Over 15 Years Index • 33.3% FTSE Actuaries Index-Linked Over 5 Year Index 	0.75%

Pensions Committee, 24 September 2013

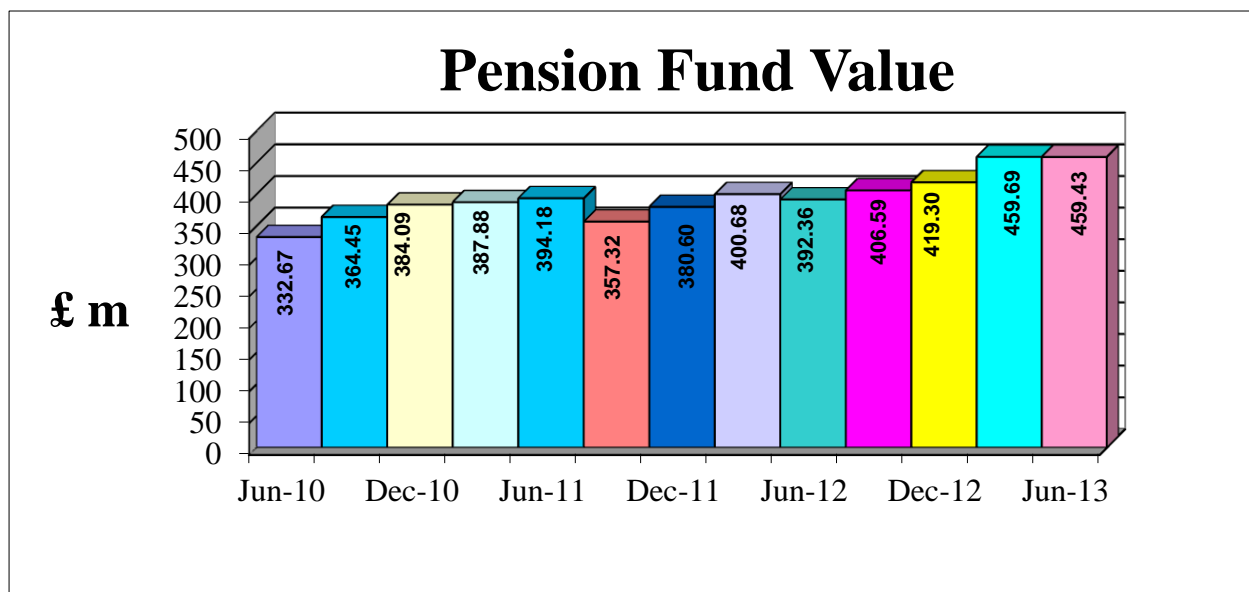
Manager and % of target fund allocation	Mandate	Tactical Benchmark	Out performance Target
UBS 10%	Property	IPD (previously called HSBC/AREF) All Balanced Funds Median Index	To outperform the benchmark
Ruffer 10%	Multi Asset	Not measured against any market index – for illustrative purposes LIBOR (3 months) + 4%.	To outperform the benchmark
State Street (SSgA) 5%	Sterling Liquidity Cash Fund	7-day LIBID	To outperform the benchmark

- 1.5 UBS, SSgA and Baillie Gifford manage the assets on a pooled basis. Standard Life, 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.
- 1.6 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).
- 1.7 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 is the Multi Asset (Ruffer) and the Passive Equity (SSgA) Managers who will attend two meetings per year, one with Officers and one with Pensions Committee. However if there are any specific matters of concern to the Committee relating to the Managers performance, arrangements can be made for additional presentations.
- 1.8 Hyman’s performance monitoring report is attached at **Appendix A. (exempt report)**

2. Fund Size

- 2.1 Based on information supplied by our performance measurers the total combined fund value at the close of business on 30 June 2013 was **£459.43m**. This valuation differs from the basis of valuation used by our Fund Managers and our Investment Advisor in that it excludes income. This compares with a fund value of £459.69m at the 31 March 2013; a **decrease** of £0.26m. The movement in the fund value is attributable to an increase in cash of £0.71m and a decrease in fund performance of - £0.97m. The

internally managed cash level stands at **£3.90m** of which an analysis follows in this report.



Source: WM Company (Performance Measurers)

2.2 An analysis of the internally managed cash balance of **£3.90** follows:

<u>CASH ANALYSIS</u>	<u>2011/12</u>	<u>2012/13</u>	<u>2013/14</u>
	£000's	<u>Updated</u> £000's	<u>30 Jun 13</u> £000's
Balance B/F	-8495	-1194	-3474
Benefits Paid	31123	31272	8685
Management costs	1606	1779	174
Net Transfer Values	-58	-1284	192
Employee/Employer Contributions	-30194	-30222	-9373
Cash from/to Managers/Other Adj.	4869	-3780	-90
Internal Interest	-45	-45	-16
Movement in Year	7301	-2280	-428
Balance C/F	-1194	-3474	-3902

2.3 As agreed by members on the 27 June 2012 a cash management policy has now been adopted. The policy sets out that should the cash level fall below the de-minimus amount of £2m this should be topped up to £4m. This policy includes drawing down income from the bond and property manager.

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 30.06.13	12 Months to 30.06.13	3 Years to 30.06.13	5 years to 30.06.13
Fund	-0.4%	16.6%	11.2%	6.2%
Benchmark return	-1.3%	12.9%	10.4%	7.1%
*Difference in return	1.0%	3.3%	0.8%	-0.8%

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 + 2.6%) is shown below:

	Quarter to 30.06.13	12 Months to 30.06.13	3 Years to 30.06.13	5 years to 30.06.13
Fund	-0.4%	16.6%	11.2%	6.2%
Benchmark return	-5.1%	-1.8%	10.8%	11.5%
*Difference in return	5.0%	18.7%	0.4%	-4.7%

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 30 JUNE 2013)

	Standard Life	Royal London	UBS	Ruffer	SSgA	Baillie Gifford ¹
QUARTER						
Return (performance)	1.3	-4.9	0.3	-0.8	-0.1	1.7
Benchmark	-1.7	-5.6	1.4	0.1	-0.1	-0.1
*Over/(Under) Performance vs. Benchmark	3.0	0.7	-0.2	-0.9	0.0	1.8
TARGET	-1.2	-5.4	n/a	n/a	n/a	n/a
* Over/(Under) Performance vs. Target	2.4	0.5	n/a	n/a	n/a	n/a

Source: WM Company, Fund Managers and Hymans

Pensions Committee, 24 September 2013

¹ Trading commenced 25 April so not trading for the full period. Target is measured using annualised data, so not yet applicable.

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

ANNUAL PERFORMANCE (LAST 12 MONTHS)

	Standard Life	Royal London	UBS	Ruffer	SSgA	Baillie Gifford
ANNUAL						
Return (performance)	27.6	5.1	-10.8	12.3	21.2	27.5
Benchmark	17.9	3.0	1.7	0.6	21.3	21.2
*Over/(Under) Performance vs. Benchmark	8.2	2.1	-12.5	11.6	-0.1	6.3
TARGET	19.9	3.7	n/a	n/a	n/a	n/a
* Over/(Under) Performance vs. Target	6.1	1.3	n/a	n/a	n/a	n/a

Source: WM Company, Fund Managers and Hymans

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

4. Fund Manager Reports

4.1. UK Equities (Standard Life)

- Representatives from Standard Life are due to make a presentation at this committee therefore a brief overview of their performance as at 30 June 2013 follows.
- The value of the fund as at 30 June saw an increase in value of 1.20% on the previous quarter.
- Standard Life outperformed the benchmark in the quarter by 3.0% and outperformed the target in the quarter by 2.4%. Since inception they are below benchmark by -0.4% and -2.4% against the target.

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

- Representatives from Royal London are due to make a presentation at this committee therefore a brief overview of their performance as at 30 June 2013 follows.
- The value of the fund as at 30 June 2013 saw a decrease of 4.5% on the previous quarter.

Pensions Committee, 24 September 2013

- c) The fund achieved a net return of 4.8% during the quarter which was above the benchmark by 0.7% and above the target by 0.5%. Since inception they outperformed the benchmark by 0.6% and outperformed the target by 0.1%.

4.3. Property (UBS)

- a) In accordance with agreed procedures officers met with representatives from UBS on the 19 August 13 at which a review of their performance as at 30 June was discussed.
- b) The value of the UBS portfolio fund saw a negligible decrease in value of since the previous quarter.
- c) UBS delivered a return of 0.3% but underperformed the benchmark by 1.1% over the quarter. The Fund is behind the benchmark over the year by 12.5%.
- d) In June 2013, UBS received new investments totalling £197.5m from three UK Pension Funds. Other Clients also withdrew their redemption requests from the queue. This enabled UBS to revoke the liquidation notice issued earlier in the year. This has removed the immediate sale pressures and allows the portfolio to be managed as a going concern.
- e) UBS also mentioned that they were looking at modernising the fund with regard to the on-going governance of the fund. UBS explained that they have commissioned John Forbes Consulting to review the fund governance with a view to making proposals for change later in the year. The review will look at:
- Fund structure and regulatory impact
 - Oversight of key decisions and independent representation
 - Mechanisms for creation of new units and redemptions
 - Communication and transparency
 - Alignment of interests and conflict management
 - Liquidity, valuations and unit pricing
- f) UBS were asked to explain what the reasons were for undertaking a modernisation of the fund. They explained that the governance arrangements are out of date as they were originally set up in the 1990's. They believe that the new governance arrangements will protect the fund from instability due to the run of withdrawals experienced previously. One of the options being considered is the introduction of a maximum withdrawal amount in a given period.
- g) UBS were asked to explain what caused the significant underperformance over the past year. They explained that the performance was mainly due to the movement in the Net Asset Value of the Fund, a 16% reduction in values. This was due to historically low levels of transactions in the market and that asset values did not reflect the real values. Once the transactions started to go through more accurate values were then used.

Pensions Committee, 24 September 2013

- h) As well as looking at the modernising the fund, UBS outlined the future stating that they believe the fund has a potential to deliver outperformance of 9% p.a. over the next five years. This will be achieved by increasing rents or redeveloping existing properties. They added that they are eager to deliver performance through excellent asset management and new purchases.
- i) The number of properties in the fund currently stands at 34 and a void rate of 7.8%.
- j) The retained portfolio following implementation of their current sales programme will have a total number of properties of 28 and a void rate of 3.7%.
- k) During the last quarter they have completed a purchase of a cinema complex in Richmond and currently going through the legal process at the moment is the purchase of two supermarkets.
- l) No whistle blowing issues or governance was reported.

4.4. 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. Ruffer attended their last meeting with members at the 26 June 13 Pensions Committee meeting. Officers met with representatives from Ruffer on the 13 February 2013.
- b) Ruffer underperformed the benchmark in the quarter by -0.9% but has outperformed the benchmark in the year by 11.6%.

4.5. 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 members on the 12 December 2012 and officers met with representatives from SSgA on the 20 May 2013, at which a review of their performance as at 31 March 13 was discussed.
- b) As expected the portfolio performed in line with the benchmark over the quarter.
- c) Members agreed at the Pensions Committee on the 26 March 2013 to transfer £20m into a SSgA cash fund on a short term basis pending the implementation of the strategy to reduce exposure to equities and increase exposure to multi assets. This decision was driven by risk diversification and preservation of capital. On advice received from Hymans £20m was transferred from the MPF passive equity portfolio to the MPF Sterling Liquidity Fund during May 2013.

Pensions Committee, 24 September 2013

- d) The MPF Sterling Liquidity Fund policy is to maintain safety of principal by investing in short-term money market instruments and fixed deposits. It is a Pooled fund and is measured against a benchmark of 7-day LIBID.

4.6. Global Equities Manager (Baillie Gifford)

- a) In accordance with agreed procedures officers met with representatives from Baillie Gifford on the 19 August 13 at which a review of their performance as at 30 June was discussed.
- b) The value of the Baillie Gifford portfolio fund saw an increase in value of 1.72% since the previous quarter.
- c) Baillie Gifford have outperformed the benchmark over the quarter by 1.8% (net of fees) and outperformed the benchmark by 3.2% (net of fees) over the last year. Since inception they have outperformed the benchmark by 2.9%.
- d) Baillie Gifford stated that the positive performance came from a wide range of stock contributors and no major detractors.
- e) Their fund positioning remains unchanged in it that they will continue to increase exposure to technology & innovation and the focus in Emerging Markets shifted from infrastructure to consumer- oriented companies.
- f) Current positioning of the portfolio has holdings in Growth Stalwarts (strong Brands) 26%, Rapid Growth (fastest growth) 24%, Cyclical Growth (longer term performance) 35%, Latent Growth (stocks most out of favour with the markets) 13% and cash of 2%.
- g) Baillie Gifford confirmed that there had been no strategy changes and they were continuing to focus on growth and in particular the potential growth in technology and innovation stocks. They also mentioned that the focus in Emerging Markets shifted from infrastructure to consumer-oriented companies.
- h) Baillie Gifford were asked if the philosophy of increasing exposure to technology has met their expectations and they explained that over the short term the results are fairly neutral and still too early in the process to tell but reiterated that it is all part of a long term strategy.
- i) Baillie Gifford's outlook for the portfolio over the longer term indicates that bouts of volatility may continue but believes this provides opportunity for stock pickers. They will continue to search for companies which are in good shape but believe that their stock driven approach is well placed to capitalise on long term opportunities.
- j) No governance or whistle blowing issues were reported.

4.7 WM Performance Measurers

Officers met with a WM representative on the 19 August 2013 who gave a presentation on the 2012/13 returns of the WM universe (all other LGPS funds). A summary of the major points are as follows:

- WM universe is made up of 85 funds.
- The benchmark for the universe was 13.8%.
- The WM Universe data shows that on average funds have been reducing allocations to UK Equities and increasing allocations to Overseas Equities with North America and Emerging Markets being the main focus. In the Bond markets funds have been reducing allocations to Index Linked Bonds and increasing exposure to overseas Bonds. There is a slowdown into alternatives and an increase into Diversified Growth Funds (i.e. Balanced Funds - multi assets).
- Three quarters of the funds in the universe outperformed the WM benchmark.
- Havering Pension Fund return was 14.6% and outperformed the universe benchmark by 0.7%. The outperformance can be attributed to the effects of asset allocation of 0.2% and stock selection of 0.5%.
- A positive decision in asset allocation (the split between asset classes of equities, bonds etc) means that the fund invested more than the benchmark in an area that has performed well or invested less in an area that has performed poorly.
- Stock selection will be positive if the fund has outperformed the benchmark in a particular area (Stocks are selected by the various Fund Managers). Holdings in Equities were the largest contributor but were negated by the poor performance in Property.
- Havering Pension Fund achieved an overall ranking for the year of 32nd.

	2012/13	3 Yrs	5 Yrs	10 Yrs
Fund Return	14.6	8.7	6.0	8.5
Benchmark (WM Universe)	13.8	8.1	6.5	9.4
Relative Return	0.7	0.6	-0.5	-0.8
Ranking	32	34	65	82

- WM also produced charts that show the relationship between the absolute level of return achieved and the risk taken in obtaining that return for the main assets classes. Chart showed that the Havering Pension Fund had achieved increased levels of return whilst maintaining a moderate risk level when compared with other funds in the WM universe.

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 is available for scrutiny in the Members Lounge.
2. Consider a sample of all votes cast to ensure they are in accordance with the policy and determine any Corporate Governance issues arising.
3. Receive quarterly information from the Investment Managers, detailing new Investments made.
 - Points 1 and 3 are contained in the Managers' reports.
 - With regard to point 2, Members should select a sample of the votes cast from the voting list supplied by the managers placed in the Member's room 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:

Standard Life and Royal London

- 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.

Pensions Committee, 24 September 2013

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 and Social Inclusion Implications and risks:

None arising directly

BACKGROUND PAPERS

Standard Life Quarterly report to 30 June 2013
Royal London Quarterly report to 30 June 2013
UBS Quarterly report to 30 June 2013
Ruffer Quarterly report to 30 June 2013
State Street Global Assets reports to 30 June 2013
The WM Company Performance Review Report to 30 June 2013
Hyman's Monitoring Report to 30 June 2013