Havering
LONDON BOROUGH

PENSIONS COMMITTEE 20 SEPTEMBER 2016

Subject Heading:	**PENSION FUND PERFORMANCE MONITORING FOR THE QUARTER ENDED JUNE 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 30 June 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 30 June 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 30 June 2016 was **4.5%.** This matches the tactical benchmark and represents an under performance of -7**.0%** against the strategic benchmark.

The overall net return of the Fund's investments for the **year** to 30 June 2016 was **5.6%.** This represents under performance of **-2.4%** against the tactical combined benchmark and under performance of **-17.1%** 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 Funds Bonds Manager (Royal London) and from the Fund's Multi-Asset Manager (Ruffer).
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 Return	15%	Ruffer	Segregated	Active	LIBOR+
Property	5%	UBS	Pooled	Active	IPD All balanced (property) Fund's median +
Gilt/Investment	17%	Royal London	Segregated	Active	• 50% iBoxx £

Asset Class	Target allocation	Investment Manager/ product	Segregated /pooled	Active/ Passive	Benchmark and Target
Bonds					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.

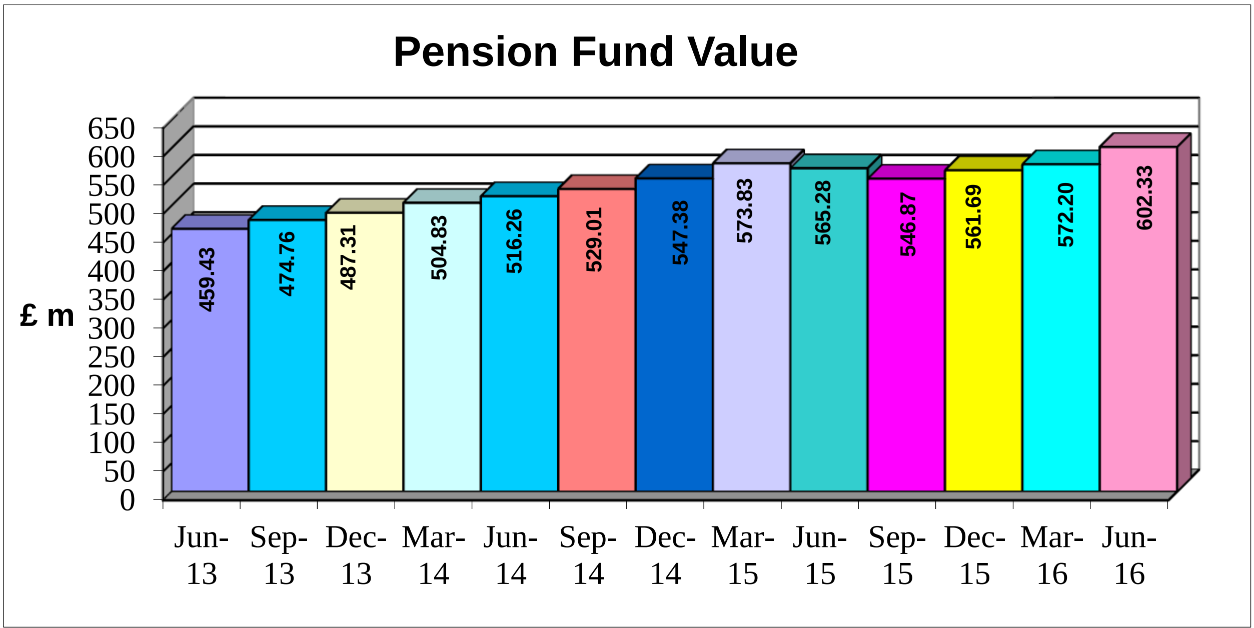
1.7 Since 2006, to ensure consistency with reports received from our Performance Measurers, Investments Advisors and Fund Managers, the 'relative returns' (under/over performance) calculations has been changed from the previously used arithmetical method to the industry standard geometric method (please 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 30 June 16 was **£602.33m**. 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 £572.20m at the 31 March 16; an **increase** of **£30.13m**. The movement in the fund value is attributable to an increase in assets of £26.23m and an increase in cash of £3.90m. The internally managed cash level stands at **£15.55m** of which an analysis follows in this report.



Source: WM Company (Performance Measurers)

2.2 An analysis of the internally managed cash balance of **£15.55m** follows:

CASH ANALYSIS	**2014/15 31 Mar 15**	**2015/16 31 Mar 16 Updated**	**2016/17 30 Jun 16**
	£000's	£000's	£000's
Balance B/F	**-5661**	**-7599**	**-12924**
Benefits Paid	33568	35048	8831
Management costs	1600	1754	192
Net Transfer Values	-135	518	138
Employee/Employer Contributions	-35306	-42884	-13559
Cash from/to Managers/Other Adj.	-1618	306	1796
Internal Interest	-47	-67	-22
Movement in Year	**-1938**	**-5325**	**-2624**
Balance C/F	**-7599**	**-12924**	**-15548**

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 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 30.06.16	12 Months to 30.06.16	3 Years to 30.06.16	5 years to 30.06.16
Fund	4.5%	5.6%	7.8%	8.0%
Benchmark	4.4%	8.1%	7.8%	7.6%
*Difference in return	0.0%	-2.4%	0.0%	0.3%

Source: WM Company

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

3.2 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 30.06.16	12 Months to 30.06.16	3 Years to 30.06.16	5 years to 30.06.16
Fund	4.5%	5.6%	7.8%	8.0%
Benchmark	12.4%	27.4%	18.0%	16.2%
*Difference in return	-7.0%	-17.1%	-8.6%	-7.1%

Source: WM Company

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

3.3 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 2016)

Fund Manager	Return (Performance)	Benchmark	Performance vs benchmark	Target	Performance vs Target
Royal London	8.77	9.22	**-0.45**	9.41	**-0.64**
UBS	0.81	0.12	**0.69**	n/a	**n/a**
London CIV/Ruffer	3.70	0.10	**3.60**	n/a	**n/a**
SSgA Global Equity	8.73	8.75	**-0.02**	n/a	**n/a**
SSgA Fundamental Index	8.57	8.55	**0.02**	n/a	**n/a**
SSgA Sterling Liquidity Fund	0.14	0.09	**0.05**	n/a	**n/a**
London CIV/Baillie Gifford (Global Alpha Fund)	6.90	8.80	**-1.90**	9.43	**-2.53**
London CIV/Baillie Gifford (DGF)	0.90	1.00	**-0.10**	n/a	**n/a**
GMO	0.34	0.61	**-0.27**	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	15.67	16.56	**-0.89**	17.31	**-1.64**
UBS	9.01	7.18	**1.83**	n/a	**n/a**
London CIV/Ruffer	0.40	0.50	**-0.90**	n/a	**n/a**
SSgA Global Equity	13.91	13.91	**0.00**	n/a	**n/a**
SSgA Sterling Liquidity Fund	0.54	0.36	**0.18**	n/a	**n/a**
London CIV/Baillie Gifford (Global Alpha Fund)	11.70	13.90	**-1.90**	16.40	**-4.70**
London CIV/Baillie Gifford (DGF)	0.40	4.00	**-3.50**	n/a	**n/a**
GMO	-5.05	0.42	**-5.47**	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

4. Fund Manager Reports

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

a) Representatives from Royal London are due to make a presentation at this Committee therefore a brief overview of their performance as at 30 June 2016 follows.

b) The value of the fund as at 30 June 16 increased by £10.66m on the previous quarter.

c) The fund achieved a net return of 8.77% during the quarter and under-performed the benchmark for the quarter by -0.45%. Royal London under-performed the benchmark over the one year period by 0.89%. Since inception they outperformed the benchmark by 0.53%.

d) 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.

4.2. Property (UBS)

a) In accordance with agreed procedures officers met with representatives from Royal London on the 17 August 2016 at which a review of their performance as at 30 June 16 was discussed.

b) The value of the fund as at 30th June 2016 increased by £0.2m since the previous quarter.

c) UBS delivered a return of 0.8% over the quarter, outperforming its benchmark by 0.7%. The Fund is ahead of the benchmark over the year by 1.8% and 1.7% over 3 years. But is behind over the five year period to 30thJune 2016 by -1.9%.

d) The number of properties in the fund currently stands at 31 with a void rate of 5.87%. Student accommodation in Newcastle has achieved completion and is now being let, thereby further reducing voids in the fund.

e) As at the 30th June 2016 there is 9.6% leverage (maximum of 10% permitted), but reduced to 5.5% as at 31st July 2016. The majority of this was bridging debt which will be reduced once the sale of UBS-CLOVA is completed at the end of August 2016. They have an attractive debt agreement with a strong strategy in place to repay the debt.

f) UBS were pleased to announce the new appointment of a Director of UK Business Development, Global Real Estate, Asher Garnett in April 2016. He is responsible for growing UBS's client and product franchise and for ensuring its real estate capabilities are marketed across the UK. Asher joins UBS from global investment management firm, Blackrock (2010-2016) where he worked in real estate and alternative investments. Asher was introduced to officers at the meeting.

g) There were no sales completed in the last quarter.

h) The Fund has purchased three new properties this quarter, a prime office building on a garden square in London W.1., which was comprehensively refurbished in 2014. This is a core holding to the fund. A purpose built student accommodation in Belfast providing 156 studios within 5 minute walk from Queens University campus, this was a genuine off market deal which increase weighting to alternatives. Lastly a multi let industrial estate in Swanley, built in the 1970's and extensively refurbished in 2009/10. This property is based on a junction of the M25 and the M20 serving both south east London and the greater south east region. This was another core holding for the fund.

i) Performance was mainly driven by the Funds strategically overweight position in Central London and the industrial sector. UBS's current strategy is to continue to retain its overweight position in retail warehousing, industrial and London offices and to increase its exposure to alternative real estate. In this quarter they have again increased their weighting in alternatives by purchasing the student accommodation in Belfast, which provides good sustainable rental income, with very low voids and relatively low risk.

j) We asked if there has been any activity that was planned during the year which has not progressed as expected, they said that planning permission for the redevelopment of the Leisure World, Southampton property (a fully let prime 10 acre waterfront site), has been delayed, the planning meeting is now scheduled for October this year. All other projects are on track.

k) UBS were asked the reason why the fund had taken on some level of debt and their arrangements for paying this debt down. They said that they used the debt to purchase the Student accommodation in Belfast, they said that they negotiated a very attractive debt agreement, and plan to repay most of this debt when the sale of UBS-CLOVA completes at the end of August 2016. This leverage was always only intended as a short term bridging debt. We asked if they considered continuing the use of debt in the fund given the current low interest rates, they said that they would consider this but as they already negotiate very attractive debt agreements the low interest rates would not influence their current strategy.

l) UBS's redemption notices served on the Fund remained under 1% at the end of June 2016; we asked if the fund has seen any recent changes in redemption levels since then and if there have been any liquidity issues within the fund. They said that the redemption levels have remained the same at around £6 million, but they said that they have new investors joining the fund to the value of 20mil which more than offsets the redemptions. The new money they are raising will also offset some of their remaining debt. They had no liquidity issues.

m) UBS said that they do not envisage any impact on the funds strategy following the outcome of the EU referendum.

n) No whistle blowing issues or governance was reported.

4.3. Multi Asset Manager (Ruffer)

a) Representatives from Ruffer are due to make a presentation at this Committee therefore a brief overview of their performance as at 30 June 2016 follows.

b) The value of the fund as at 30 June 16 increased by £2.66m on the previous quarter.

c) Ruffer delivered a return of 3.70% (net of fees) over the quarter, outperforming the benchmark by 3.60%. Over the last 12 months Ruffer delivered a return of -0.40% underperforming the benchmark by -0.90%.

d) £70.7m of assets were transferred to the London CIV on the 21 June 2016. The residual assets of £1.3m were transferred on the 31 August 2016.

e) The London CIV will oversee the monitoring and review of the performance of this mandate. However Ruffer has stated that they will continue with the existing monitoring arrangements and meet with the Committee to report on its own performance.

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 increased by £6.2m since the last quarter.

c) 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.

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

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. Representatives from the London CIV have been invited to present to the Pensions Committee meeting on the 13 December 2016 to provide a performance update on the Baillie Gifford (Global Equities) mandate.

b) The value of the fund increased by £5.8m over the last quarter.

c) The Global Alpha Fund delivered a return of 6.9% (net of fees) over the quarter, underperforming the benchmark by -1.9%. Over the last 12 months Baillie Gifford delivered a return of 11.7% underperforming the benchmark by -1.9%.

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

e) The London CIV will oversee the monitoring and review of the performance of this mandate and representatives from the London CIV have been invited to present to the Pensions Committee meeting on the 13 December 2016 to provide the review on the Baillie Gifford (Global Alpha Equities) mandate.

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) The value of the fund increased by £0.3m over the last quarter.

c) The Diversified Growth Fund delivered a return of 0.9% (net of fees) over the quarter, underperforming the benchmark by -0.1%. Over the last 12 months the Diversified Growth Fund delivered a return of 0.4% underperforming the benchmark by -3.5%.

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

e) The London CIV will oversee the monitoring and review of the performance of this mandate and representatives from the London CIV have been invited to present to the Pensions Committee meeting on the 13 December 2016 to provide the review on the Baillie Gifford (Diversified Growth Fund) mandate

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. 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. GMO last met with the members of the Pension Committee on the 16 June 2016 at which they covered the period ending up to 31 March 2016.

b) The value of the fund increased by £0.3m over the last quarter.

c) The fund achieved a net return of 0.03% during the quarter and underperformed the benchmark for the quarter by -0.02%. Over the last 12 months GMO delivered a return of -5.05% underperforming the benchmark by -5.5%.

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 for the quarter was 45% Equities, 13% Alternative strategies, 6.9% Fixed Income and 34.9% Cash/Cash Plus.

4.8. WM Performance Measurers

a) Officers met with a WM representative on the 17 August 2016 who gave their annual presentation on the returns of the WM universe (other LGPS funds) and how the Havering Fund performed compared to the universe. A summary of the major points for the 2015/16 performance are as follows:

- WM universe is made up of 88 funds with a combined asset value of £207billion.
- The benchmark for the universe was 0.2%.

- Havering Pension Fund return was -1.0% and underperformed the universe benchmark by -1.2%.

- Havering Pension Fund achieved an overall ranking for the year of 73rd.

b) The Havering Fund is structured differently from the average fund as shown in the table below :

Asset Allocation	**Universe**	**Havering**
Equities	60	27
Bonds	16	21
Multi Asset	3	30
Cash	3	3
Alternatives	9	13
Property	9	6

c) The performance can be attributed to the effects of asset allocation, with Multi-asset strategies having a disappointing year and were the main contributor to the funds underperformance, over the medium term the funds absolute returns remain strong and are in excess of the strategic benchmark.

	2015/16	**2014/15**	**3 Yrs**	**5 Yrs**	**10 Yrs**
Fund Return	-1.0	13.3	6.3	7.5	4.9
Benchmark (WM Universe)	**0.2**	**13.2**	**6.4**	**7.1**	**5.6**
Relative Return	-1.2	0.1	-0.1	0.4	-0.7
Ranking	73	51	56	33	73

d) WM also produced charts that showed:

- 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 lower risk than other funds in the WM universe and relative risk had been rewarded,

- The long term performance of the fund's annual return against the retail price index. Over the 3, 5 10 & 20 year periods the fund outperformed inflation. Over the 20 year period the fund's capital growth outperformed inflation by 4%p.a.

e) WM summarised 2015/16 as a difficult year in general as 'riskier' assets struggled in a volatile environment. The weakness of Sterling protected UK investors from much lower returns on non-domestic investments. The fund sits within the top third of the universe over 5 years. However, this has fallen back over the shorter term period.

f) WM has made the decision to discontinue providing performance measurement services to third party clients in the UK, effective from March 2016. The production of all universe analysis including the Local authority peer group analysis will also be discontinued. They will still continue to provide their core performance measurement to State Street clients who subscribe to their custody and/or accounting services.

g) The Havering Pension Fund subscribes to both the custody and accounting services so performance measurement will continue for our fund.

The London CIV is leading on the issue of obtaining alternative service providers to produce the universe data.

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:

  Royal London (Bonds Manager) and Ruffer (Multi asset Manager).

- 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 30 June 2016
UBS Quarterly report to 30 June 2016
Ruffer Quarterly report 30 June 2016
State Street Global Assets report to 30 June 2016
Baillie Gifford Quarterly Reports 30 June 2016
GMO Quarterly Report 30 June 2016
The WM Company Performance Review Report to 30 June 2016