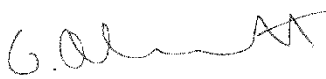




Report to:	Pensions Committee	Date:	5 September 2016
Report title:	Investment Performance of the Fund Managers to 30 June 2016		
Report from:	Gerald Almeroth, Strategic Director – Resources		
Ward/Areas affected:	Borough Wide		
Chair of Committee/Lead Member:	Councillor Sunita Gordon		
Author(s)/Contact Number(s):	Lyndsey Gamble, Head of Financial Strategy and Planning extn 5358 Lisa Doswell, Treasury and Investments Manager extn 5354		
Corporate Plan Priorities:	<ul style="list-style-type: none"> • A Smart Council 		
Open/Exempt:	Open Appendix B Exempt By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972.		
Signed:			Date: 24 August 2016

1. Summary

- 1.1. This report shows the performance of the Pension Fund Investment Managers for the quarter ending 30 June 2016, performance in the last twelve months, annualised rolling three year performance against target benchmark and performance since inception.

2. Recommendation

That the pension Committee is recommended to:

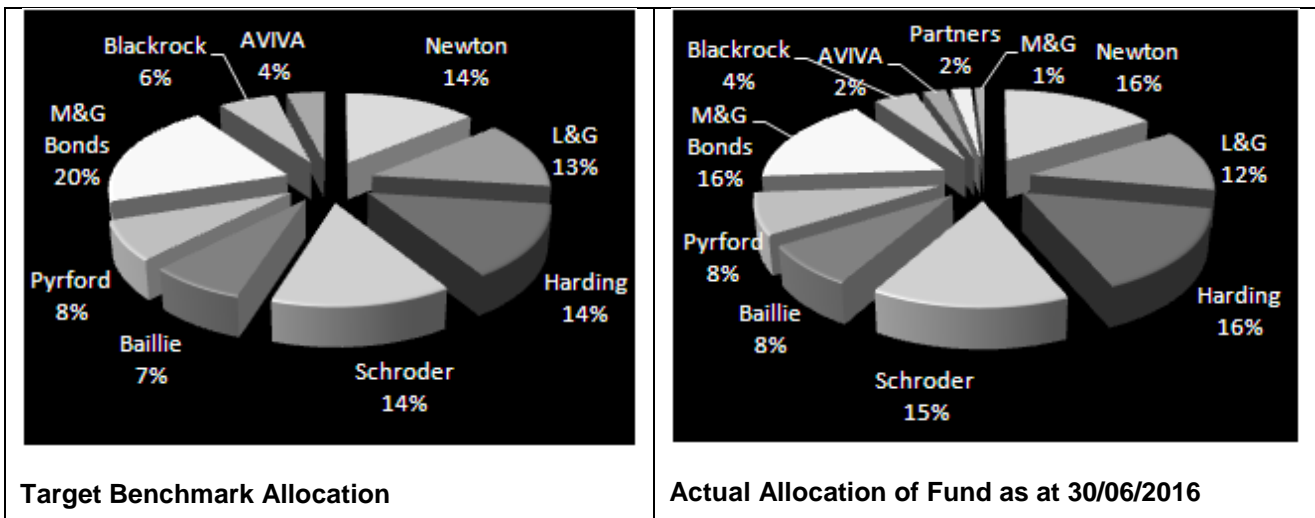
- 2.1 Note the performance of the Pension Fund Investment Managers.

3. Background

- 3.1 Legal & General (L&G), Newton Investment Management (Newton), Harding Loevner, Schroder, Baillie Gifford, Pyrford, M&G, BlackRock and Partner's Group were employed as the Council's investment managers for the year ending 30 June 2016. The Council was also invested in two separate funds; M&G UK Companies Financing Fund and Aviva Investors UK Real Estate Fund of Funds Plan. In December 2015 the Fund agreed a new residential property mandate with Invesco. There has been no investments made into this fund as yet. The first drawdown is expected by the end of September.



3.2 Under the Council’s current investment strategy a target benchmark allocation of 42% of the total fund value is to be invested in global equities managed in separate, equal sized portfolios by Newton, Harding Loevner and Schroder’s. 13% of the fund is to be invested in UK equities by L&G and 15% of the fund is to be split equally in absolute return pooled vehicles managed by Baillie Gifford and Pyrford. 20% of the fund is currently targeted in bonds by M&G, however there is a long term strategic target to bonds of 15% and 5% to infrastructure, but this will take some time to implement. 10% of the fund is targeted in Property, split between 6% with BlackRock and 4% with AVIVA. This is shown in the chart on the left, against the current actual allocation of the fund on the right.



3.3 Actual allocations against the target are monitored on a regular basis. Potential courses of action are discussed with Hymans Robertson if material variations occur.

3.4 Performance targets for all fund managers are set by the Council to obtain good investment performance returns, whilst also balancing risk. The targets set are in line with the overall investment strategy agreed by the Pension Fund Working Party in March 2011.

4 Performance of the Managers

4.1 The tables set out within the report show the manager’s performance for the quarter, over the last twelve months and since inception (where possible) and a comparison against the relevant indices in the Council’s strategic asset allocation benchmark. All figures are shown net of fees. Appendix C (exempt information) shows the basis on which fees are calculated by each fund manager and the fees which have been incurred for the current and previous quarter.

4.2 The investment performance monitoring service transitioned from WM to Northern Trust (The Fund’s custodian) and this is the sixth quarter in which Northern Trust’s performance data has been used to produce this report.

Movement in Fund Value from 31 March 2016 to 30 June 2016

4.3 The table below shows the value of holdings with each of the fund managers as at the end of the latest quarter and the end of the previous quarter.

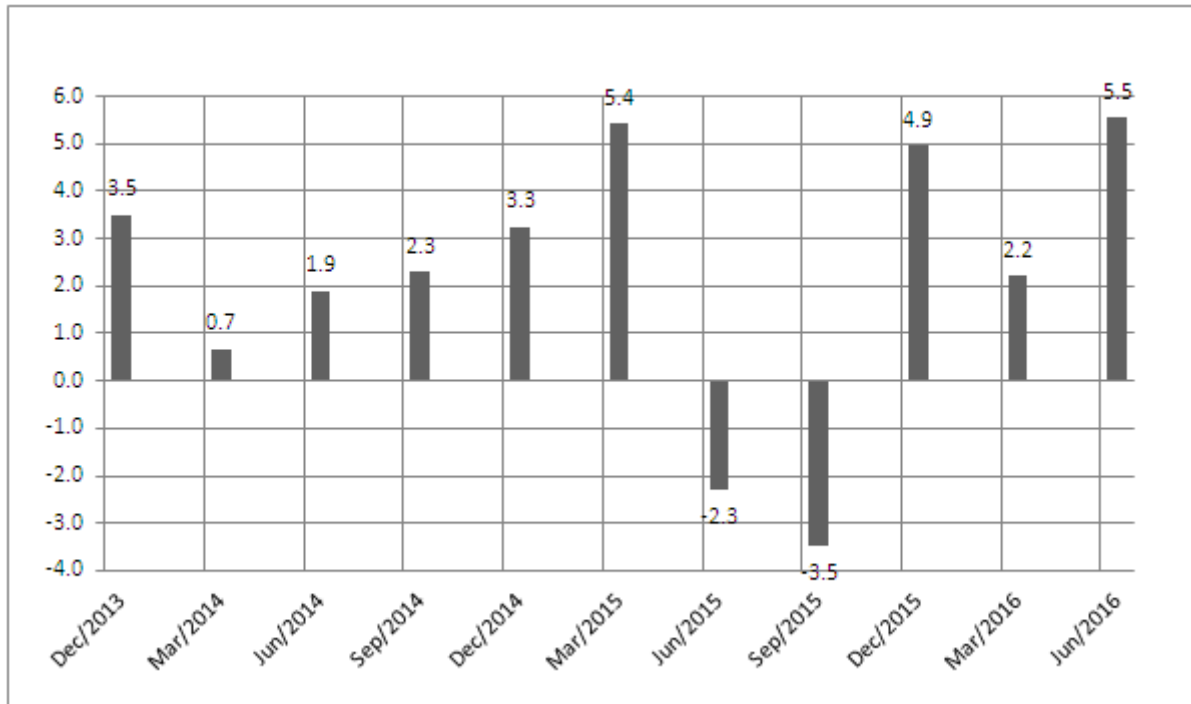


Fund Manager	Value at end 31/03/16 £'000	Value at end 30/06/16 £'000	Value change £'000	% Change
Total Equities	284,438	304,986	20,548	7.2
Legal & General	58,308	61,072	2,764	4.7
Newton	79,057	84,192	5,135	6.5
Harding Loevner	75,221	82,310	7,089	9.4
Schroder	71,852	77,412	5,560	7.7
Bonds	81,777	86,361	4,584	5.6
M&G bonds	81,777	86,361	4,584	5.6
Pooled Multi Asset	79,582	80,883	1,301	1.6
Baillie Gifford	40,265	40,458	193	0.5
Pyrford	39,317	40,425	1,108	2.8
Property	34,479	34,772	293	0.8
BlackRock	22,224	22,530	306	1.4
AVIVA	12,255	12,242	-13	-0.1
Alternatives	15,036	15,725	1,834	13.2
Partner's Group	10,113	10,722	609	6.0
M&G – Co's Financing Fund	3,778	3,858	80	2.1
Cash	12,231	12,716	485	3.9
Total Assets	507,543	535,443	27,900	5.5



The chart below shows the percentage change in the total value of the fund each quarter.

Fund Value Movement %



The above table excludes cash.

4.4 TOTAL FUND PERFORMANCE

Total fund performance pre and post strategy implementation

Benchmark 42 months to 31/10/12	Fund 42 months to 31/10/12	Variance	Benchmark 42 months to 30/06/16	Fund 42 months to 30/06/16	Variance
%	%	%	%	%	%
12.5	11.1	-1.4	9.2	9.6	0.4

4.5 Prior to the new strategy implementation the combined fund underperformed the benchmark by 1.4% over the previous 42 months (benchmark 12.5%, actual 11.1%). Looking at performance 42 months after the new strategy was implemented the combined fund outperformed the benchmark by 0.4% (benchmark 9.2%, actual 9.6%).



Total fund performance for the latest quarter ended 30 June 2016

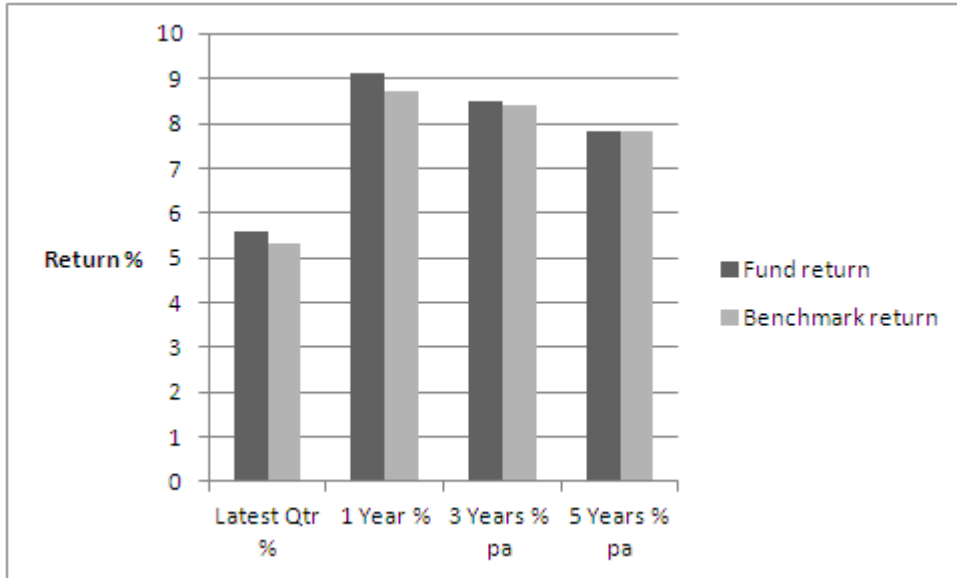
TOTAL FUND	Target Allocation	Fund Allocation	Benchmark Return	Fund Return	Variance
	%	%	%	%	%
Equities	55	59	7.7	7.2	-0.5
Bonds	20	16	4.6	5.6	1.0
Pooled Multi Asset	15	16	0.9	1.6	0.7
Property	10	6	0.1	1.1	1.0
Alternatives	0	3	n/a	n/a	n/a
TOTAL ASSETS	100.0	100.0	5.3	5.6	0.3

- 4.6 At total fund level the combined fund performance outperformed the benchmark over the period achieving a return of 5.6% compared to the benchmark return of 5.3%. Performance of individual asset classes is detailed in paragraph 4.9 onwards.

Total fund performance – longer term

TOTAL FUND	1 Year	3 Years	5 Years
	% pa	% pa	% pa
Fund return	9.1	8.5	7.8
Benchmark return	8.7	8.4	7.8
Variance %	0.4	0.1	0.0

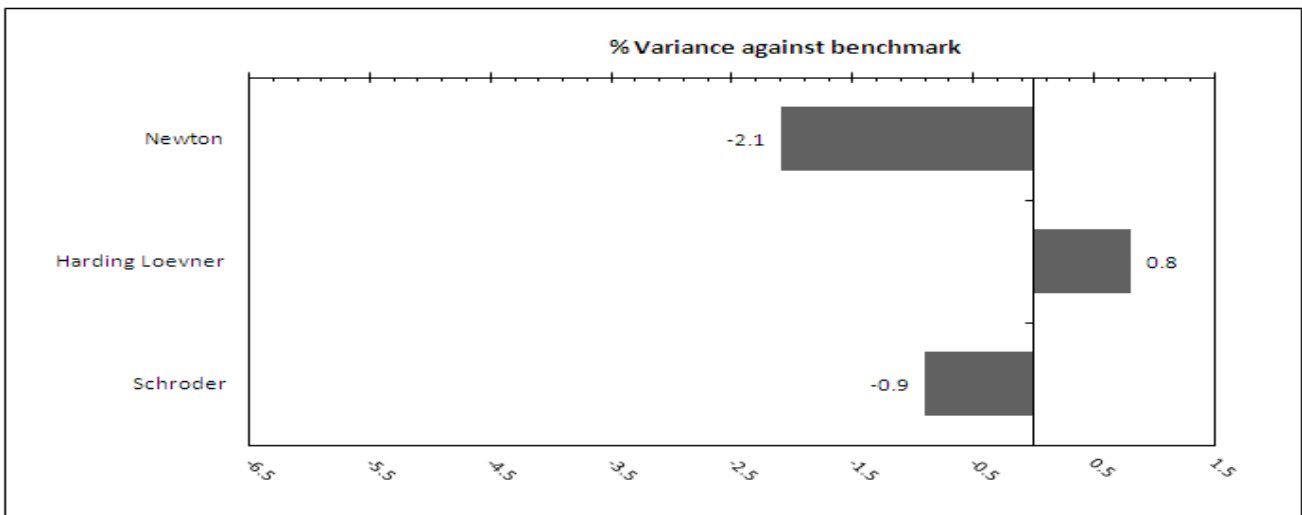
- 4.7 At total fund level, as at June 2016 the combined fund outperformed the benchmark by 0.4% over the past year, by 0.1% per annum over the past three years and matched the benchmark over the past five years.
- 4.8 The bar chart below summarises the overall performance of the fund over the latest one year, three year and five year positions.



4.9 EQUITY PERFORMANCE

Equity performance for the latest quarter ended 30 June 2016

Manager	Target Allocation	Fund Allocation	Benchmark Return	Fund Return	Variance
	%	%	%	%	%
L&G	13	12	4.7	4.7	0.0
Newton	14	16	8.6	6.5	-2.1
Harding Loevner	14	16	8.6	9.4	0.8
Schroders	14	15	8.6	7.7	-0.9
TOTAL EQUITIES	55	59	7.7	7.2	-0.5





- 4.10 Global markets made a confident start to the quarter, but there was considerable volatility in the run-up to and immediate aftermath of the UK referendum on membership of the EU. The vote to leave initially shook the markets, with currency markets being most affected and Sterling significantly weakened. A UK recession and property collapse was anticipated and fears spread to the rest of the EU. However, by the end of the quarter global equity indices began to reverse the downward trend and the FTSE 100 had reached a new high for 2016. While equity markets experienced volatility globally, in particular, financials across the UK and Europe were very weak. The only major developed market to outperform the broad index was North America and emerging markets as a whole remained relatively stable.
- 4.11 As shown in table 4.9, Newton underperformed the benchmark. Their main areas of weakness were in the technology and energy sectors. A number of large technology holdings including Apple and Microsoft were relatively weak performers. Oil and mining stocks, in which Newton is underweight performed well. Harding Loevner slightly outperformed the benchmark. They benefitted from good stock selection in healthcare and information technology. They were also underweight in the Eurozone, which was the worst performing region. Schrodgers underperformed the benchmark during the quarter. This performance is attributed to their value approach, which is not ideally positioned for the low volatility, high yield stocks that continue to do well. However their rebalancing methodology is effective at taking advantage of market volatility and they expect to benefit from this going forward.

Equity performance – longer term

Manager	Benchmark Return 1 Year	Fund Return 1 Year	Variance	Benchmark Return Since Inception	Fund Return Since Inception	Variance
	%	%	%	%	%	%
L&G	2.2	2.2	0.0	6.3	6.3	0.0
Newton	13.3	13.3	0.0	13.1	14.8	1.7
Harding Loevner	13.3	17.5	4.2	13.1	14.2	1.1
Schrodgers	13.3	8.8	-4.5	13.1	11.8	-1.3

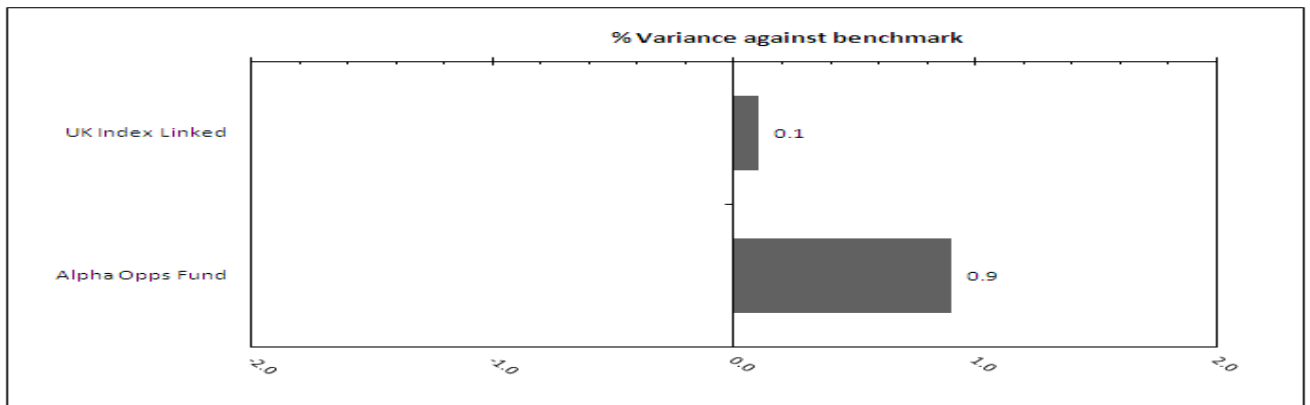
- 4.12 As shown in the table above, over the longer term both L&G and Newton matched the benchmark during the twelve months ended June 2016. Harding Loevner showed outperformance and Schrodgers underperformed. Since inception, L&G matched the benchmark, Newton and Harding Loevner outperformed the benchmark and Schrodgers underperformed.



4.13 BOND PERFORMANCE

Bond performance for the latest quarter ended 30 June 2016 (M&G)

	Target Allocation	Fund Allocation	Benchmark Return	Fund Return	Variance
	%	%	%	%	%
UK Index Linked	8	8	11.1	11.2	0.1
Alpha Opportunities Fund	12	8	0.1	1.0	0.9
TOTAL (Weighted Average)	20	16	4.6	5.6	1.0



4.14 10-year UK government bond yields plunged at the end of March to a record low by the end of June. The majority of this fall occurred after the result of the referendum was announced, driven mainly by expectations of a cut in UK interest rates. These moves resulted in strong gains for gilts, especially longer-dated instruments which are the most sensitive to falling yields. UK investment grade corporate bonds generally delivered solid gains over the quarter as well, although this was driven by the strong performance of government bond markets. While credit spreads widened sharply after the vote, they narrowed in the final days of June and ended the quarter only slightly wider than they were at the end of March.

4.15 The Index-Linked fund benefitted from holding positions in index-linked gilts maturing in 20 and 40 years which outperformed other index linked bonds.



Bond performance – longer term

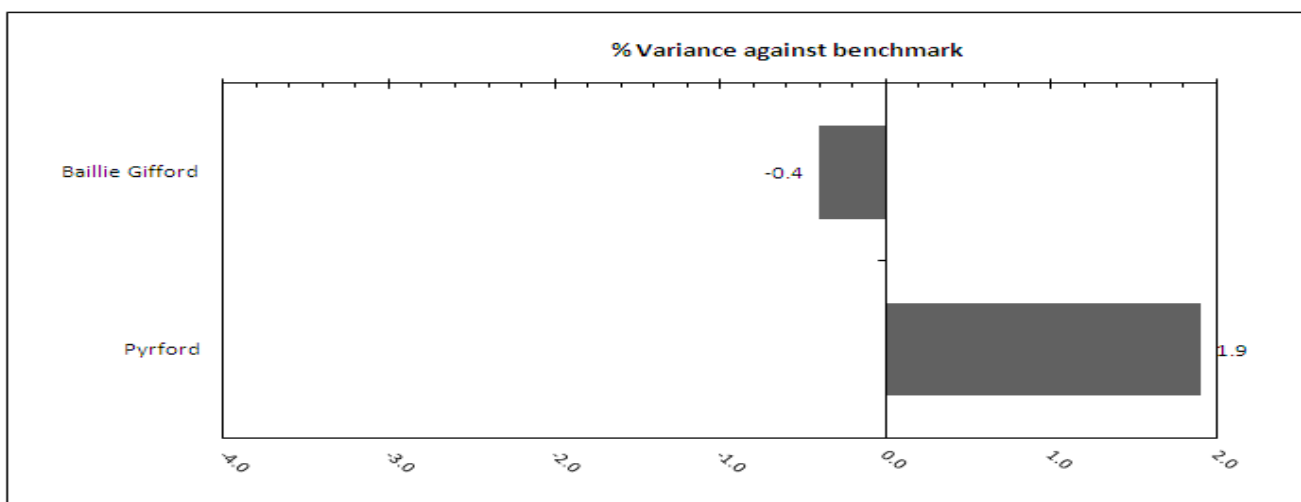
Manager	Benchmark Return 1 Year	Fund Return 1 Year	Variance	Benchmark Return Since Inception	Fund Return Since Inception	Variance
	%	%	%	%	%	%
UK Index Linked	17.0	17.6	0.6	10.9	11.9	1.0
Alpha Opportunities Fund	0.6	0.4	-0.2	1.4	0.9	-0.5

4.16 As shown in the table above, over the longer term the M&G Index Linked Fund outperformed the benchmark during the twelve months ended June 2016, whilst the Alpha Opportunities Fund underperformed. The UK Index Linked Fund also outperformed since inception and the Alpha Opportunities Fund underperformed.

4.17 POOLED MULTI-ASSET PERFORMANCE

Pooled Multi-Asset Performance for the latest quarter ended 30 June 2016

Manager	Target Allocation	Fund Allocation	Benchmark Return	Fund Return	Variance
	%	%	%	%	%
Baillie Gifford	7.5	7.8	0.9	0.5	-0.4
Pyrford	7.5	7.7	0.9	2.8	1.9
TOTAL POOLED MULTI-ASSET	15.0	15.5	0.9	1.6	0.7





- 4.18 Baillie Gifford assets were transferred from five underlying boroughs into the London Collective Investment Vehicle (CIV) on 15 February 2016. This was the first such transfer for the London Borough of Sutton towards the pooling of investment assets. Following this, on the 17 June 2016 Pyrford became Sutton’s second fund manager to transfer into the CIV.
- 4.19 Over the quarter Baillie Gifford underperformed the benchmark. This is largely due to the performance of holdings in listed equities, property and structured finance, which they attribute to the post Brexit shocks across risk markets. Pyrford’s outperformance has been attributed to holdings equities, particularly overseas holdings, which were boosted by Sterling weakness. Their holdings in short duration overseas government bonds also contributed positive returns in the quarter.

Pooled Multi-Asset Performance – longer term

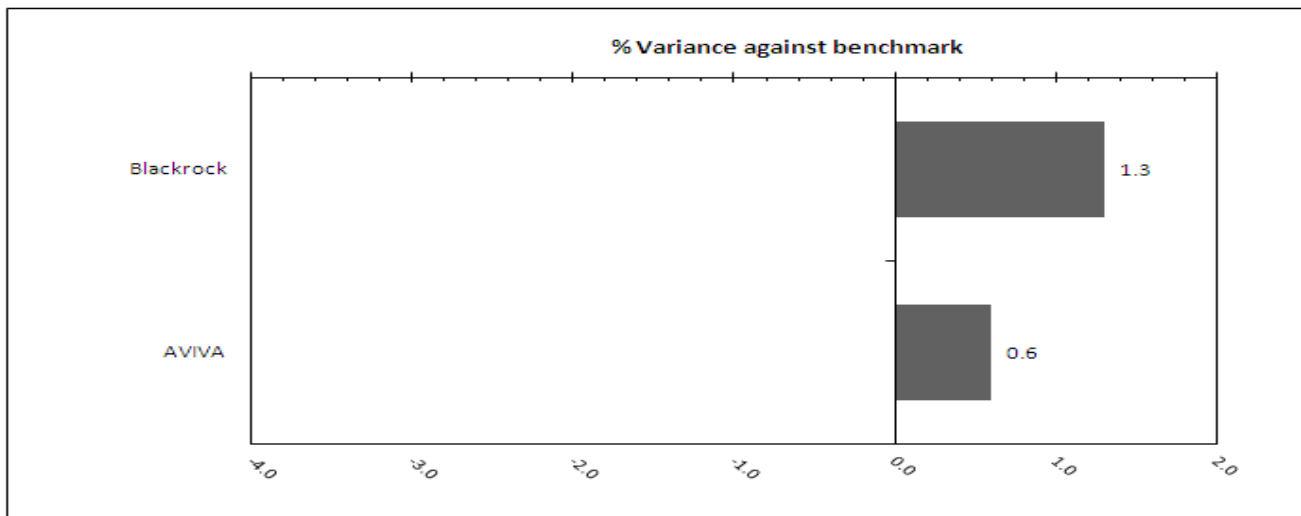
Manager	Benchmark Return 1 Year	Fund Return 1 Year	Variance	Benchmark Return Since Inception	Fund Return Since Inception	Variance
	%	%	%	%	%	%
Baillie Gifford	3.7	-0.4	-4.1	3.6	4.1	0.5
Pyrford	3.7	7.2	3.5	3.6	4.1	0.5

- 4.20 Baillie Gifford underperformed the benchmark while Pyrford outperformed the benchmark during the twelve months ended June 2016. Both outperformed since inception.

4.21 PROPERTY PERFORMANCE

Property Performance for the latest quarter ended 30 June 2016

Manager	Target Allocation	Fund Allocation	Benchmark Return	Fund Return Income	Fund Return Capital	Total Fund Return	Variance
	%	%	%	%	%	%	%
BlackRock	6	4	0.1	0.9	0.5	1.4	1.3
AVIVA	4	2	0.1	0.8	-0.2	0.6	-0.6



4.22 The EU referendum vote was so close to quarter end that the independent valuers have been unable to assess the full impact of the resultant uncertainty on property values. Returns from the UK commercial property market therefore held up during the quarter. The industrial sector was the biggest outperformer. It is likely to be one of the sectors least affected by Brexit, with Sterling weakness offering the prospect of a boost to manufacturing and exports.

4.23 During the quarter BlackRock and AVIVA both outperformed the benchmark. BlackRock did not complete any acquisitions during the quarter. They completed three sales totalling £142.1m, including the remaining properties in the BlackRock Workspace Property Trust (BWPT) to Westbrook Partners. BWPT was established in 2011 to acquire multi-let office and industrial properties located within improving areas of Greater London. This transaction brought the joint venture to an end after what BlackRock views as 5 successful years. AVIVA's best performing investments were THREE Enhanced Debt Fund and AEW South East Office Fund. These are new funds and returns have been relatively low to date, as they have been incurring costs in their investment periods, but performance has improved now that they are largely through their acquisition phases.

Property Performance – longer term

Manager	Benchmark Return 1 Year	Fund Return 1 Year	Variance	Benchmark Return Since Inception	Fund Return Since Inception	Variance
	%	%	%	%	%	%
RREEF/Blackrock	7.2	7.8	0.6	4.1	4.1	0.0
AVIVA	7.2	6.7	-0.5	8.5	8.4	-0.1

4.24 As shown in the table above, Blackrock outperformed and AVIVA underperformed the benchmark during the twelve months ending June 2016. BlackRock matched the benchmark since inception and AVIVA underperformed the benchmark since inception.



4.25 ALTERNATIVES PERFORMANCE

Alternatives Performance for the latest quarter ended 30 June 2016

Manager	Benchmark Allocation	Fund Allocation	Fund Return
	%	%	%
Partner's Group – Infrastructure	0	2	6.0
M&G – UK companies financing fund	0	1	1.6

- 4.26 Partner's Group and M&G are not measured as part of the fund's overall strategic benchmark. Due to the way investment is made with Partner's Group, it is not meaningful to make comparisons with their performance target at this stage.

Alternatives Performance – longer term

Manager	Fund Return 1 Year	Fund Return Since Inception
	%	%
Partner's Group	25.8	7.5
M&G	3.8	4.7

5 ANNUALISED ROLLING 3 YEARS TO 30 JUNE 2016

- 5.1 The annual performance targets for equities, bonds and pooled multi-asset fund managers are set over a rolling three year period. Since M&G (Bonds) were appointed in May 2014 this assessment will start for the quarter ended 30/06/17.

Manager	3 Yr Benchmark Return	Target 3 Yr Benchmark Return	3 yr Fund Return	Variance against Benchmark	Variance against Target
	%	%	%	%	%
Newton	10.6	12.6	11.4	0.8	-1.2
Harding Loevner	10.6	13.6	12.9	2.3	-0.7
Schroder	10.6	13.6	8.7	-1.9	-4.9
Baillie Gifford	3.6	6.6	3.7	0.1	-2.9
Pyrford	3.6	6.6	3.7	0.1	-2.9



- 5.2 The above table shows that over the three year rolling period all managers except for Schroders have outperformed the benchmark, however all managers have underperformed the target benchmark over the same period. The underperformance from Schroders is likely to be due to their value based approach which does not perform well in current market conditions.

6 Options Considered

- 6.1 Not applicable

7 Impacts and Implications

Financial

- 7.1 The financial implications are addressed within the report.

Legal

- 7.2 There are no legal issues arising from this report.

8 Appendices and Background Documents

Appendix Letter	Title
A B	Current Investment Strategy Benchmarks and Targets Manager Fees (Exempt By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972)

Background Documents
Northern Trust Investment Performance Reports

Audit Trail		
Version	Final	Date: 24 August 2016
Consultation with other officers		
Officer	Comments Sought	Comments checked by
Finance	Yes	Lyndsey Gamble
Legal	N/A	N/A

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