



Haringey Council

Agenda item:

Pensions Committee

On 22 February 2011

Report Title. **Fund Performance update**

Report of **Director of Corporate Resources**

Signed : *J. Power* 10/2/11

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Wards(s) affected: **All**

Report for: Noting

1. Purpose of the report

- 1.1. To consider the latest investment performance data for the Pension Fund and for each of the Fund's investment managers.
- 1.2. To report on key responsible investment issues using information provided by the Fund Managers and the Local Authority Pension Fund Forum (LAPFF).
- 1.3. To report on budget monitoring against the Pension Fund budget.
- 1.4. To report on late payments of contributions to the Pension Fund.

2. Introduction by Cabinet Member

- 2.1 Not applicable.

3. State link(s) with Council Plan Priorities and actions and /or other Strategies:

- 3.1. Not applicable.

4. Recommendations

- 4.1 That the Fund performance position as at end of December 2010 be noted.
- 4.2 That the responsible investments information provided be noted.
- 4.3 That the pension fund budget monitoring position be noted.
- 4.4 That the late payments of contributions be noted.

5. Reason for recommendations

- 5.1. This report is for noting.

6. Other options considered

- 6.1. Not applicable.

7. Summary

- 7.1 The investment return achieved in the quarter to December 2010 was 5.24%, which was 0.57% behind the benchmark and 0.98% behind the target. The Fidelity bonds portfolio is the only one to have met or exceeded the target since the inception of the investment strategy in April 2007.
- 7.2 The budget monitor shows an overall variance of £6.55m at the end of December 2010, mainly due to the change in the timing of contributions paid by the Council to the Pension Fund.

8. Head of Legal Services Comments

- 8.1 The Head of Legal Services has been consulted on the content of this report. There are no specific legal comments on the report which is for noting.

9. Equalities & Community Cohesion Comments

- 9.1. There are no equalities issues arising from this report.

10. Consultation

- 10.1. Not applicable.

11. Service Financial Comments

11.1 Performance of the Fund Managers continues to be carefully monitored in the current market conditions. The investment strategy of the Fund is being reviewed during this year, which will address the performance issues.

11.2 The switch to the separate Pension Fund bank account in October has resulted in a change to the timing of the payment of the Council's contributions into the Fund. This has impacted on the budget monitoring position at the end of December 2010, but will be fully accounted for in the year end accounts.

12. Use of appendices /Tables and photographs

12.1 Appendix 1: Fund holdings and top ten equity holdings.

12.2 Appendix 2: Fund performance to 31 December 2010.

12.3 Appendix 3: Responsible Investment update.

12.4 Appendix 4: Budget Management: monitoring to 31 December 2010.

13. Local Government (Access to Information) Act 1985

Northern Trust performance monitoring reports.

Fund performance update report to Pensions Committee on 20th December 2010.

14. Previous Quarter Investment performance

14.1 The investment performance of the Pension Fund was last reported to Pensions Committee in December 2010. That report covered the period up to 30 September 2010, at which time the following points were noted:

- Since monitoring against the new benchmark commenced on 1 April 2007, the combined Haringey fund had increased slightly in absolute terms by 0.45% per cent up to 30 September 2010, underperformed the gross benchmark by 2.26% and also underperformed the gross target by 3.90%.
- The performance by the Fund Managers over the same period was as follows:
 - Fidelity's Bond mandate out performed the gross target by 0.92% and the Equity mandate under performed the gross target by 2.08%.
 - Capital's Equity and Bond mandates were below target by 3.00% and 1.65% respectively.
 - ING were below target by 1.96%.

15. Total Fund investment performance for quarter to 31st December 2010

15.1 The current investment strategy was implemented on 1st April 2007 and so all the performance figures which follow show performance since that date.

15.2 Performance of the combined Haringey fund compared to benchmark and target for the three months to end of December 2010 and annualised performance from 1 April 2007 to end of December 2010 are shown below. The target is shown gross of Fund Managers fees and assumes that returns above benchmark are achieved evenly throughout the year.

	3 months to end of Dec 2010	1 April 2007 to 31 Dec 2010 (annualised)
	%	%
Overall fund performance	5.24	1.80
Benchmark	5.81	4.04
Performance versus benchmark	(0.57)	(2.24)
Overall fund performance	5.24	1.80
Target	6.22	5.68
Performance versus target	(0.98)	(3.88)

15.3 This shows that in the period to 31st December 2010:

- The annualised performance of the combined Haringey fund since 1 April 2007 was a small increase in absolute terms of 1.80%, the fund under performed the benchmark by 2.24% and under performed the target by 3.88%;
- The annualised position has improved very marginally since the report to the last meeting with the under performance versus target decreasing from (3.90%) to (3.88%).

15.4 The cash held in-house has been invested in line with the Treasury Management Strategy Statement for 2010/11 – see the cash management section below.

15.5 Appendix 1 shows how the value of the Fund was split into the various types of investments at the end of December 2010 and for comparison the end of the previous quarter. The top ten equity holdings include the whole of the Fund's exposure to equities including both directly held shares and those in pooled funds.

16. Fund Manager Performance

- 16.1 Appendix 2 shows investment performance to the end of December 2010 for each Fund Manager, compared to benchmarks and targets as supplied by the custodian, Northern Trust. The data covers the period since 1 April 2007 when the current investment strategy was implemented.
- 16.2 The performance targets for each Fund Manager's mandate are shown below together with the fund managers' performance against those benchmarks since 1 April 2007 when the strategy was implemented. The contract with Legal & General has been in place for less than two years and so long term performance data is not available. However their portfolio is invested in line with the benchmark, so the variation from the benchmark is minimal. The variation has amounted to +0.06% since the contract started.
- 16.3 There have been 52 calls on the Pantheon Asia, Europe and USA funds totalling £19.9 million to date. There have been no distributions yet. Private equity is a long term asset class and therefore performance numbers are excluded as they are not considered meaningful when the funds are still in the drawdown phase.
- 16.4 Targets are set out in the table below and are gross of fees.

	% Target above benchmark	% annualised performance above / (below) benchmark in the period 1 Apr 07 to 31 Dec 10	% annualised performance above/ (below) target in the period 1 Apr 07 to 31 Dec 10
Capital - equities	2.0	(1.03)	(3.03)
Capital - bonds	1.0	(0.74)	(1.74)
Fidelity - equities	1.7	0.13	(1.57)
Fidelity - bonds	0.6	1.40	0.80
ING - property	1.0	(1.10)	(2.10)
Pantheon – private equity	0.75	N/A	N/A

- 16.5 The latest quarterly meetings took place in February 2010 between each active Fund Manager and the Head of Finance: Treasury & Pensions. A summary of the key issues discussed at those meetings is set out below.

Capital International

- Performance to date.
- Future outlook for markets.
- Review of Responsible Investment issues.

Fidelity

- Performance to date.
- Future outlook for markets.
- Review of Responsible Investments Issues.

ING

- Performance to date.
- Volatility in the property market and future estimated returns.

Pantheon

- Performance to date.
- Future outlook for markets.
- Future pattern of cash flows.

17. Conclusions

- 17.1 Since monitoring against the benchmark commenced on 1 April 2007, the annualised performance of the combined Haringey fund has shown a small increase in absolute terms of 1.80% up to 31 December 2010. During this period the Fund under performed the gross benchmark by 2.24% and under performed the gross target by 3.88%.
- 17.2 Capital and ING are underperforming against both the benchmark and the target. Fidelity have outperformed the benchmark and target in the bonds portfolio, but the equity portfolio performance has been below both the benchmark and target.
- 17.3 Investment returns in the equity markets were positive in the quarter, but in bond markets the returns were negative. There are a number of ongoing issues which are likely to impact on future performance, and the situation will continue to be monitored carefully. These include:
- Sovereign debt issues, particularly in the Eurozone;
 - The price of oil and commodities;
 - The trends of inflation and risks of deflation;
 - Interest rates;
 - Property prices and rental values.

18. Responsible Investments

- 18.1 At Pensions Committee on 23 June 2008 a review of the Fund's Responsible Investment Policy was considered and agreed by members. One of the recommendations was that officers monitor the fund managers' approach to the revised Responsible Investment Policy. The Fund is a member of the Local Authority Pension Fund Forum (LAPFF) which provides information about responsible investment issues and undertakes engagement with companies on these issues on behalf of local authorities.
- 18.2 Appendix 3 compares responsible investment information provided by the Council's three equity Fund Managers for the quarter ending 31 December 2010 with the information supplied by LAPFF over the same time period. This highlights engagement work on environmental and governance issues.

19. Budget Management

- 19.1 The budget monitoring analysis to the end of December 2010 is shown in detail in Appendix 4. In overall terms the variance was £6.55m
- 19.2 The significant variances to date are:
- Since the introduction of the separate Pension Fund bank account in October 2010, contributions from the Council to the Fund are paid only when they become due in the month following deduction from salaries, rather than being automatically transferred. This means that there is one month's worth less contributions than budgeted for, which amounts to £3.5m. This will be fully accounted for in the year end accounts.
 - Transfers in and out of the Fund continue to be volatile, as the volume and timing varies throughout the year;
 - Investment income was £3.2m less than budgeted as the value of dividends paid by companies continues to remain low in the current economic climate;
 - Investment management expenses are significantly lower than budgeted at this stage in the year due to the timing of the receipt of invoices from fund managers.

20. Cash Management

- 20.1 The Pension Fund is holding cash in-house for a number of reasons:
- Funding property investments – it was agreed in 2007 at the last investment strategy review to increase the allocation of the Fund to property. An amount of £18m was invested in cash to fund this. The balance still to be drawn down is £1.4m.
 - Funding private equity investments – at the last investment strategy review it was agreed that in addition to the original allocation, £10m a year be allocated

to private equity and that this should be funded from cash surpluses and kept in cash pending drawdown. To date £19.9m has been drawn down and £15.7m remains in cash.

- Reduction in bond holdings – at the Committee meeting on 15th April 2010, it was decided to reduce the Fund’s holdings in bonds and invest in cash. Bonds were sold and cash of £29.5m was transferred to the in-house account.

20.2 The elements of the cash invested in-house at the end of December 2010 can be summarised as follows:

Property allocation	£1.4m
Private equity allocation	£15.7m
Sale of bonds	£29.5m
Other surplus of contributions over benefits	£15.6m
Total	£62.2m

20.3 The table below shows key statistics, which are used for the Council’s treasury management reporting, applied to the pension fund cash investments during the quarter. Descriptions of the statistics are provided below:

		Q 30 Jun	Q 30 Sept	Q 31 Dec
A	Credit score – value weighted	2.88	3.55	3.69
B	Credit score – time weighted	4.12	4.26	4.27
C	Weighted Average Maturity (days)	81	85	91
D	Interest Rate earned	0.64%	0.65%	0.75%

A & B: These measures score credit risk on a scale of 0 to 10 on both a value weighted and a time weighted basis and the table below demonstrates how to interpret the scores:

Above target	AAA to AA+	Score 0 - 2
Target score	AA to A+	Score 3 - 5
Below target	Below A+	Score over 5

C: This is a measure of how liquid the portfolio is. It shows the weighted average maturity of the fixed term deposits. In addition the Fund holds instant access funds in money market funds.

D: This is the interest rate earned in the quarter on the deposits placed.

20.4 The statistics show that the cash is invested in highly rated institutions with an average maturity of 91 days, up slightly from 85 days at the end of the previous quarter. This level of liquidity allows the Pension Fund to pay drawdowns to the property and private equity managers as required while investing long enough to achieve a reasonable rate of return. 0.75% was the rate earned which was 0.25% higher than the Bank of England base rate.

21. Late payment of contributions to the Pension Fund

21.1 It was agreed by the Committee at the last meeting that those employers paying contributions after the deadline of no more than 19 days after the end of the month in which they were deducted, would be reported in this report on a quarterly basis.

21.2 The table below shows the late payment of contributions relating to the period October to December 2010:

	Occasions late	Average Number of days late	Average monthly contributions
Europa	2	22	£800
TLC	3	4	£6,300

21.3 Europa is in a transition phase of handing over their contract to their parent company and it is anticipated the situation will improve at that point. Officers have written again to TLC and will continue to press the issue with the backing of the Pensions Administration Strategy. The amounts of interest due as a result of these delays total less than £5 and therefore it remains uneconomic to invoice the employers for this. The situation will continue to be monitored and reported back to the Committee.

Appendix 1

a) Fund Holdings

Fund Holdings	As at 31 December 2010			As at 30 September 2010		
	Market Value £'000		% of Fund	Market Value £'000		% of Fund
UK equities		191,496	27.1%		180,364	26.7%
held in individual shares	36,019			37,210		
held in pooled funds	155,477			143,154		
Overseas equities		254,648	36.1%		230,177	34.1%
held in individual shares	95,581			85,010		
held in pooled funds	159,067			145,167		
Bonds		126,629	18.0%		129,165	19.2%
held in individual bonds	27,558			27,882		
held in pooled funds	99,071			101,283		
Property	49,513	49,513	7.0%	47,475	47,475	7.0%
Private Equity	17,802	17,802	2.5%	18,818	18,818	2.8%
Cash		65,538	9.3%		69,033	10.2%
held by Fund Managers	3,337			2,750		
held in-house	62,201			66,283		
Totals		705,626	100.0%		675,032	100.0%

b) Top Ten equity shares - held directly and in pooled funds

Company	Sector	As at 31 December 2010		
		Rank	Percentage of Equities	Market Value
			%	£m
Royal Dutch Shell	Oil & Gas	1	3.29%	14.70
HSBC	Banks	2	2.40%	10.70
Vodafone	Telecomms	3	2.11%	9.41
BP	Oil & Gas	4	1.77%	7.90
Glaxosmithkline	Pharmaceuticals	5	1.50%	6.69
BG Group	Oil & Gas	6	1.46%	6.53
Rio Tinto	Mining	7	1.31%	5.83
BHP Billiton	Mining	8	1.28%	5.70
Astrazeneca	Pharmaceuticals	9	1.05%	4.69
British American Tobacco	Tobacco	10	0.98%	4.37

Appendix 2

Fund Performance to 31st December 2010

Gross of Fees

	Market valuations 31.03.08	Market valuations 31.03.09	Market valuations 31.03.10	Market valuations 31.12.10	Weighted % Fund change 1 Oct to 31 Dec 2010	% benchmark change 1 Oct to 31 Dec 2010	% target 1 Oct to 31 Dec 2010	Under (-)/over (+) performance versus target 1 Oct to 31 Dec 2010	Weighted % Fund change 1 April 2007 to 31 Dec 2010	% benchmark change 1 April 2007 to 31 Dec 2010	% target 1 April 2007 to 31 Dec 2010	Under (-)/over (+) annualised performance versus target 1 April 2007 to 31 Dec 2010
	£'000	£'000	£'000	£'000	%	%	%	%	%	%	%	%
Capital -Equities	125,246	95,609	139,785	150,224	8.47	8.71	9.21	(0.74)	3.56	4.59	6.59	(3.03)
Capital -Fixed Income	62,451	63,111	70,923	44,427	(1.51)	(0.99)	(0.74)	(0.77)	5.46	6.20	7.20	(1.74)
Fidelity -Equities	126,566	98,171	144,909	152,482	10.47	8.53	8.96	1.51	4.46	4.33	6.03	(1.57)
Fidelity - Fixed Income	65,390	64,390	77,481	82,361	(2.03)	(2.03)	(1.88)	(0.15)	7.79	6.39	6.99	0.80
Bernstein -UK Equity	117,805	71,622	-	-	-	-	-	-	-	-	-	-
Bernstein -Global Equity	28,299	18,875	-	-	-	-	-	-	-	-	-	-
L & G-UK Equity	-	-	108,949	117,027	7.37	7.38	7.38	(0.01)	-	-	-	-
L & G-Global Equity	-	-	28,077	29,626	9.71	9.69	9.69	0.02	-	-	-	-
ING	51,505	36,000	46,167	49,421	1.14	1.90	2.15	(1.01)	(7.71)	(6.61)	(5.61)	(2.10)
Pantheon - private equity	2,719	11,509	13,131	17,857	(15.32)	11.07	11.82	(27.14)	-	-	N/A	N/A
Total	579,981	459,287	629,422	643,425	5.24	5.81	6.22	(0.98)	1.80	4.04	5.68	(3.88)

In house cash - earmarked for property	9,350	9,350	3,252	1,358
In house cash - earmarked for private equity	9,500	9,500	13,174	15,736
Other	544	4,154	17,504	45,107
Total Fund	599,375	482,291	663,352	705,626

Appendix 3

Comparison of Responsible Investment Activity Quarter ending 31 December 2010 Equity Fund Managers and the Local Authority Pension Fund Forum (LAPFF)

Fidelity	Capital International	Legal & General	LAPFF
<p>Environmental Issues</p> <p>Fidelity is engaging with a number of power generation companies to determine how the Energy Market Reforms which plan to decarbonise energy generation will impact on them and shareholder value. The reforms are subject to consultation at the present time and the expectation is they will be introduced in 2013.</p>	<p>Capital staff went on a research trip to China recently and took particular note of environmental issues in a number of industries including property development, car manufacturing and steel production amongst others. One specific example is that they have noted that the government is putting in measures to address the small energy inefficient and polluting steel mills.</p>	<p>Legal & General met with Tesco management during the quarter to discuss their progress on carbon reduction and how they plan to meet their aim of being carbon neutral by 2050.</p>	<p>LAPFF is supporting the Carbon Disclosure Project's Water Disclosure initiative which aims to highlight issues around water constraints and water security and encourage companies to put these issues higher on their agendas.</p>
<p>Governance / Remuneration Issues</p> <p>Fidelity has voted against the recommendation that Ramsay Health Care's compensation strategy for senior executives be approved in previous years on the basis that no performance targets were set out in the strategy. Following this feedback, the 2010 strategy included performance targets.</p>	<p>Capital met with JP Morgan during the quarter to discuss their compensation policy and other executive pay issues. This was particularly timely in the light of these issues remaining a controversial issue in the media.</p>	<p>L&G attended an investor briefing with Lloyds Banking Group and met with the Chairman to discuss their approach to corporate responsibility following the takeover of HBOS Bank. The areas the Board are looking at include financial inclusion and supporting local communities.</p>	<p>The LAPFF has been engaging with Associated British Foods for some time to address the lack of a company wide approach to corporate responsibility issues. The result of this engagement is that in December 2010 the company presented a corporate responsibility strategy to the AGM.</p>

Fidelity	Capital International	Legal & General	LAPFF
<p>Other Engagement activity</p> <p>During discussions with Oil Search Ltd, Fidelity explored the impact on the local community and issues of wealth redistribution arising from their project in Papua New Guinea.</p>	<p>Following the Liberty International de-merger of it's property business earlier this year, Capital met with the chairman of one of the new companies formed as a result. They discussed a range of issues including corporate governance and diversity.</p>	<p>A meeting was held with Glaxosmithkline to discuss their access to medicine strategy in emerging markets, which tries to balance pricing with accessibility in these markets.</p>	<p>LAPFF are currently undertaking a targeted engagement campaign with food and drink companies to discuss the risks and opportunities created by obesity.</p>
<p>Other Issues</p> <p><u>UK Investor Stewardship Code</u></p> <p>In September 2010 it was reported to the Pensions Committee that the Financial Reporting Council published the first Stewardship Code for Institutional Investors. The aim of the Code is to improve the quality of corporate governance through promoting better dialogue between shareholders and company boards and encouraging more transparency about the way investors oversee companies they own. Fund management firms have been encouraged to sign up to the code and it has been confirmed that Fidelity, Capital International and Legal & General have all published policies showing how they apply the Code.</p>			

Appendix 4

Pension Fund Budget Management - monitor at 31st December 2010

	2010/11 Budget £'000	Budget to 31 Dec 2010 £'000	Actual to 31 Dec 2010 £'000	Over/under (-) at 31 Dec 2010 £'000	Explanations of significant variations
Income					
Contributions and benefits:					
Employee Contributions	(10,700)	(8,025)	(7,023)	1,002	
Employer Contributions	(36,000)	(27,000)	(24,485)	2,515	
Transfer Values Received	(5,100)	(3,825)	(4,348)	(523)	Following the change to a separate Pension Fund bank account the Council contributions are not paid into the Fund until the month following deduction from salaries. This will be fully accounted for in the year end accounts.
Total income	(51,800)	(38,850)	(35,856)	2,994	
Expenditure:					
Pensions and other benefits	30,000	22,500	23,325	825	
Transfer values paid	5,300	3,975	5,310	1,335	
Administrative expenses	800	600	499	(101)	Transfer values are very unpredictable in terms of volume and timing.
Total expenditure	36,100	27,075	29,134	2,059	
Net addition from dealings with members	(15,700)	(11,775)	(6,722)	5,053	
Returns on Investment:					
Investment income	(15,200)	(11,400)	(8,190)	3,210	Dividends from companies continue to be low.
Taxation	190	143	114	(29)	
Investment management expenses	3,300	2,475	795	(1,680)	The timing of the submission of invoices from fund managers affects this figure.
Net return on investments	(11,710)	(8,782)	(7,281)	1,501	
Totals	(27,410)	(20,557)	(14,003)	6,554	