

Report for: Pensions Committee 14th January 2016

Item number: 12

Title: Investment Quarterly Update

Report authorised by: Tracie Evans, Chief Operating Officer (CFO)

Lead Officer: George Bruce, Head of Finance - Treasury & Pensions
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Ward(s) affected: N/A

**Report for Key/
Non Key Decision:** Non Key decision

1. Describe the issue under consideration

- 1.1 To report the following in respect of the three months to 30th September 2015:
- Investment asset values & allocation
 - Investment performance
 - Income & Expenditure
 - Communications
 - Late payment of contribution

2. Cabinet Member Introduction

- 2.1 Not applicable.

3. Recommendations

- 3.1 That the information provided in respect of the activity in the three months to 30th September 2015 is noted.

4. Other options considered

- 4.1 None.

5. Background information

- 5.1 This update report is produced quarterly. The Local Government Pension Scheme Regulations require the Committee to review investment performance on a quarterly basis and sections 13 and 14 provide the information for this. Appendix 1 shows the targets which have been agreed with the fund managers. The report covers various issues on which the

Committee or its predecessor body have requested they receive regular updates.

- 5.2 At the time of writing the report, equity markets have been highly volatile due to concerns with the slowing growth of the Chinese economy and the impact that this will have on commodities, commodity producers and exporters. Equity prices have declined sharply over the course of the year, particularly in Asia, but also USA and Europe.
- 5.3 Information on communication with stakeholders has been provided by officers in Human Resources and included in section 17.

6. Comments of the Chief Financial Officer and Financial Implications

- 6.1 The investment performance figures in section 14 show the impact of the introduction of passive fund managers in that generally the variance from target has reduced. The negative performance over three and five years reflects mainly the loss of value from the European property portfolio.

7. Comments of the Assistant Director of Corporate Governance

- 7.1 The Assistant Director of Corporate Governance has been consulted in the preparation of this report, and makes the following comments.
- 7.2 Council as administering authority for the Haringey Pension Fund (“Fund”) has an obligation to keep the performance of its investment managers under review. In this respect the Council must, at least every three months review the investments made by investment managers for the Fund and any other actions taken by them in relation to it;
- 7.3 Periodically the Council must consider whether or not to retain the investment managers. In particular members should note the continuing negative performances compared with the target benchmarks and the reason stated in this report as to why this is the case;
- 7.4 In carrying out its review proper advice must be obtained about the variety of investments that have been made and the suitability and types of investment;
- 7.5 All monies must be invested in accordance with the Council’s investment policy and members of the Committee should keep this duty in mind when considering this report and have regard to advice given to them.

8. Comments from the Independent Advisor

- 8.1 The total value of the Fund at 30 September 2015 was £976m. At 30 June 2015 the total value of the Fund was £1,012m. This reduction of £36m equivalent to approximately 4% was due to a worldwide retreat in equity markets which experienced their worst Quarter since the 2011 Euro zone

Crisis. The value of the Fund's Listed Equities fell by 7% (from £659m to £616m) between 1 July and 30 September 2015.

- 8.2 Weaknesses and issues in China (including major stock market losses, emergency Central Bank action to devalue the Renminbi and disappointing economic data) all weighed on Equity prices across the world. UK, European, North American, Japanese, Asian/Emerging Markets all saw falls over the Quarter July to September 2015. These falls were particularly pronounced in Japan and Asia/Emerging Markets.
- 8.3 By 30 November 2015 however the value of the Fund's Listed Equity investments was £658m only £1m below their value at 30 June 2015. Emerging Market Equities stabilised and the overall Equity portfolio recovered the previous Quarter's losses during the months of October and November 2015. Better than expected US corporate earnings and economic data clearly helped United States Equities increase in value over the period. European Equities were boosted by both macro economic data and statements from the European Central Bank in respect of potential further loosening of monetary policy.
- 8.4 The overall performance of the Fund over the last Quarter (to 30 September 2015), Year and Three Years is close to benchmark (see section 14.1) primarily due to the fact that the majority of the Fund is managed on a passive basis.

9. Equalities and Community Cohesion Comments

- 9.1 The Local Government Pension Scheme is a defined benefit open scheme enabling all employees of the Council to participate. There are no impacts in terms of equality from the recommendations contained within this report.

10. Head of Procurement Comments

- 10.1 Not applicable

11. Policy Implications

- 11.1 None.

12. Use of Appendices

- 12.1 Appendix 1: Investment Managers' mandates, benchmarks and targets.

13. Local Government (Access to Information) Act 1985

- 13.1 Not applicable

Total Portfolio Allocation by Manager & Asset Class

	Value 30.06.2015 £'000	Value 30.09.2015 £'000	Value 30.11.2015 £'000	Allocation 30.09.2015 %	Strategic Allocation %
Equities					
UK	164,665	154,691	162,900	15.8%	15.0%
North America	251,755	229,907	250,342	23.6%	21.7%
Europe	75,406	74,440	78,954	7.6%	7.4%
Japan	35,603	35,843	39,398	3.7%	3.5%
Asia Pacific	32,319	34,583	36,961	3.5%	3.4%
Emerging Markets	99,393	86,649	89,343	8.9%	9.0%
Total Equities	659,141	616,113	657,898	63.1%	60.0%
Bonds					
Index Linked	143,215	146,405	146,547	15.0%	15.0%
Property					
CBRE	100,225	99,061	104,378	10.1%	10.0%
Private equity					
Pantheon	35,911	41,939	40,476	4.3%	5.0%
Multi-Sector Credit					
CQS	46,108	46,052	46,425	4.7%	5.0%
Infrastructure Debt					
Allianz	19,731	20,624	22,648	2.1%	5.0%
Cash & NCA	7,949	5,840	3,152	0.6%	0.0%
Total Assets	1,012,280	976,034	1,021,524	100%	100%
Fund Managers					
Legal & General	277,690	762,511	804,438	78.1%	75.0%
BlackRock	524,668	7	2	0.0%	0.0%

The value of the fund decreased by £36 million between July and September June 2015 as equity markets gave back some of their previous gains due mainly to concerns with slowing growth in China. Volatility has continued with November valuations recovering.

The equity allocation exceeds target by 3%. This is mostly the unfunded Allianz mandate. It is anticipated that the Infrastructure debt mandate will be fully funded in 2016, this is later than originally anticipated.

14. Investment Performance Update: to 30th September 2015

Appendix 1 provides details of the benchmarks and targets the fund managers have been set. The tables below show the performance in the quarter July to September 2015 and for the 1, 3 and 5 years.

14.1 Whole Fund

	Return	Benchmark	(Under)/Out	WM LA average
Jul - Sep 2015	-3.66%	-3.49%	(0.17)%	-3.3%
One Year	2.93%	3.46%	(0.53%)	2.7%
Three Years	9.29%	9.79%	(0.50%)	8.4%
Five Years	7.89%	8.29%	(0.38%)	7.3%

One year	Return(%)	Benchmark(%)	Under/out(%)	WM LA Average(%)
Equities				
UK	-2.26	-2.30	0.04	-1.4
Developed				
Europe	-0.78	-0.80	0.02	1.3
North America	4.72	4.62	0.10	5.9
Japan	6.10	6.18	-0.08	4.9
Asia ex Japan	-11.30	-11.41	0.11	-9.4
Emerging	-12.75	-12.66	-0.09	-12.3
I L gilts	11.89	11.80	0.09	11.0
Property	12.17	14.41	-2.23	13.4
Private equity	19.15	5.77	13.38	14.8
Multi-sector				
Credit	2.34	6.19	-3.85	n/a
Total	2.93	3.46	-0.53	2.7

Five years	Return(%)	Benchmark(%)	Under/out(%)	WM LA Average(%)
Equities				
UK	6.55	6.69	-0.14	7.6
Developed				
Europe	7.45	5.80	1.64	6.8
North America	13.07	13.14	-0.07	13.2
Japan	7.31	6.38	0.93	7.8
Asia ex Japan	-0.85	1.15	-0.30	2.0
Emerging	-0.76	-2.10	1.34	-0.8
Index linked				
gilts	9.65	9.34	0.31	8.8
Property	7.88	9.71	-1.83	9.0
Private equity	12.54	13.58	-1.04	10.5
Total	7.89	8.27	-0.38	7.3

- Despite the negative returns in the last two quarters, investment returns in aggregate over the last five years have been in line with long term expectation. WM report that the ten year average local authority return to September 2015 is 6.0% p.a.
- Compared to benchmark the fund's returns have underperformed the benchmark by approximately 0.5% over 1, 3 and 5 years.
- Equity and index linked gilts, which are passively managed, show some variability compared to the benchmarks, but not significant differences.
- The main detractor from performance is property in particular overseas and more recently the overweight position in equities. Individual manager's performance is discussed below.

14.2 Legal & General Investment Management

	Return	Benchmark	Variance
Apr - Jun 2015	(7.90)%	(7.85)%	(0.05%)
One Year	(2.29)%	(2.27)%	(0.32%)
Three years	5.33%	5.90%	(0.57%)
Since inception (May 2012)	6.64%	7.18%	(0.54%)

- Total Value at 30/09/15: £762.5 million
- Variances at regional level are minimal, varying between +0.12% (Asia Pacific ex Japan) and -0.09% (UK) over the last year.
- The underperformance is due to the allocation of assets between markets being out of balance with the benchmark.

14.3 CBRE Global Investors

	Return	Benchmark	(Under)/Out
Jul - Sep 2015	1.71%	3.00%	(1.29%)
One Year	12.17%	14.41%	(2.24%)
Three Years	10.65%	12.24%	(1.59%)
Five Years	7.88%	9.71%	(1.83%)

- Total Value at 30/09/15: £105.6 million (including cash)
- The relative performance of the property portfolio over the longer term has been driven by two European holdings that have suffered significant capital loss. The UK element of the portfolio, in particular the retail element has struggled in the last 12 months.
- The two European funds have been unsuccessful. With an aggregate cost of £9.7 million, they are now valued at £0.2 million, a virtual total loss. Both funds are invested in highly leverage non prime property (German residential and Italian office / retail). The underlying holdings have suffered during the Euro crisis and the impact has been magnified on unit holders by the high levels of debt in each fund. Both funds are being rationalised which may offer an exit opportunity, but with little recovered value.
- The portfolio will lag the benchmark for many years until the impact of the two European funds passes through.

14.4 Pantheon

	Return	Benchmark	(Under)/Out	Distributions Less drawdowns
Jul - Sep 2015	8.16%	-3.90%	12.06%	-£1.99m
One Year	19.15%	5.77%	13.38%	£2.09m
Three Years	16.51%	15.43%	1.08%)	£5.87m
Five Years	12.54%	13.58%	(1.04%)	-£5.05m

- Total Value at 30/09/15: £41.9 million
- Following the first calls against the two new commitments, drawdowns exceeded distributions in the quarter, a reversal of the recent flow of cash. The 2006 / 7 vintage funds continue to distribute cash and record valuation gains as exits are achieved.
- The performance target is the MCSI Worlds plus 3.5%. The three 2006/7 vintage funds are reaching a stage when valuation gains can be expected. On average the three funds are 90% invested and 60% of the original cost has been returned. Private equity valuations tend to underestimate exit prices. It is only when the fund is substantially realised will an accurate picture of performance emerge.
- The first drawdowns have been made to the Global Secondaries and Global Select funds – total commitments \$75 million.

14.5 CQS (multi sector credit)

The CQS mandate was funded in Q3, 2015. The portfolio increased in value by £1.1 million to £46.1 million as at September 2015. Returns of 2.34% in the last year are behind the benchmark of 3 month libor plus 5.5% (6.2%).

14.6 Allianz (infrastructure debt)

The initial drawdown of £17 million was completed in Q4, with a further £3 million subsequently drawn. It is anticipated that most of the allocation will be drawn during 2016.

14.7 In house cash

	Value	Average Credit Rating	Average Maturity (days)	Return
At 30/09/15	£0.2M	AA	1	0.45%
At 30/06/15	£0.2M	AA	1	0.45%
At 31/03/15	£3.92M	AAA	1	0.38%
At 31/12/14	£2.25m	AAA	1	0.39%

15. Budget Management – 3 months to 30TH September 2015

	Prior year 2014-15 £'000	Current year 2015-16 £'000	Change in expenditure £'000
Contributions & Benefit related expenditure			
Income			
Employee Contributions	4,470	4,566	96
Employer Contributions	16,790	16,839	49
Transfer Values in	1,529	884	(645)
Total Income	22,789	22,289	(500)
Expenditure			
Pensions & Benefits	(21,548)	(21,803)	(255)
Transfer Values Paid	(1,843)	(1,214)	629
Administrative Expenses	(412)	(162)	250
Total Expenditure	(23,803)	(23,179)	624
Net of Contributions & Benefits	(1,014)	(890)	124
Returns on investment			
Net Investment Income	2,105	2,146	41
Investment Management Expenses	(1,206)	(399)	807
Net Return on Investment	899	1,747	848
Total	(115)	857	972

The fund continues to have a small surplus of income over expenditure, although that is likely to diminish later in the year.

The income shown is virtually all from property as income from other asset classes is automatically re-invested and shown within the change in market value.

16. Late Payment of Contributions

16.1 The table below provides details of the employers who have made late payments during the last quarter. These employers have been contacted and reminded of their obligations to remit contributions on time.

Employer	Occasions late	Average Number of days late	Average monthly contributions(£)
Lunchtime UK	1	1	8,200

17. Communication Policy

17.1 Two sets of regulations govern pension communications in the LGPS: The Disclosure of Information Regulations 1996 (as amended) and Regulation 67 of the Local Government Pensions Scheme (Administration) Regulations 2008 as amended.

17.2 In March 2011, the Council approved the Pensions Administration Strategy Statement (PASS). The PASS sets out time scales and procedures which are compliant with the requirements of the Disclosure of Information Regulations. The PASS is a framework within which the Council as the Administering Authority for the Fund can work together with its employing bodies to ensure that the necessary statutory requirements are being met.

17.3 In June 2008 the Council approved the Policy Statement on Communications with scheme members and employing bodies. The Policy Statement identifies the means by which the Council communicates with the Fund members, the employing bodies, elected members, and other stakeholders. These cover a wide range of activities which include meetings, workshops, individual correspondence and use of the internet. In recent times, the Pensions web page has been developed to provide a wide range of employee guides, forms and policy documents. Where possible, Newsletters and individual notices are sent by email to reduce printing and postage costs.

17.4 The requirement to publish a Communications Policy Statement recognises the importance that transparent effective communication has on the proper management of the LGPS.

Appendix 1 – Investment Managers mandates, benchmarks and targets

Manager	% of Total Portfolio	Mandate	Benchmark	Performance Target
Legal & General Investment Management	75%	Global Equities & Bonds	See overleaf	Index (passively managed)
CQS	5%	Multi Sector Credit	3 month libor + 5.5% p.a	Benchmark
Allianz	5%	Infrastructure Debt	5.5% p.a.	Benchmark
CBRE Global Investors	10%	Property	IPD UK Pooled Property Funds All Balanced Index	+1% gross of fees p.a. over a rolling 5 yr period
Pantheon Private Equity	5%	Private Equity	MSCI World Index plus 3.5%	Benchmark
Total	100%			

Asset Class	Benchmark	Legal & General Investment Management
UK Equities	FTSE All Share	15.0%
Overseas Equities		45.0%
North America	FT World Developed North America GBP Unhedged	21.7%
Europe ex UK	FT World Developed Europe X UK GBP Unhedged	7.4%
Pacific ex Japan	FT World Developed Pacific X Japan GBP Unhedged	3.4%
Japan	FT World Developed Japan GBP Unhedged	3.5%
Emerging Markets	FT World Global Emerging Markets GBP Unhedged	9.0%
Index Linked Gilts	FTA Index Linked Over 5 Years Index	15.0%
		75.0%