

Bath & North East Somerset Council

MEETING:	AVON PENSION FUND COMMITTEE
MEETING DATE:	25 SEPTEMBER 2015
TITLE:	REVIEW OF INVESTMENT PERFORMANCE (for periods ending 30 June 2015)
WARD:	ALL
AN OPEN PUBLIC ITEM	
List of attachments to this report: Appendix 1 – Fund Valuation Appendix 2 – Mercer Annual Investment Review Exempt Appendix 3 – Changes in RAG status of Managers Appendix 4 – LAPFF Quarterly Engagement Monitoring Report	

1 THE ISSUE

- 1.1 This paper reports on the investment performance of the Fund and seeks to update the Committee on routine strategic aspects of the Fund's investments and funding level. This report contains performance statistics for periods ending 30 June 2015.
- 1.2 The main body of the report comprises the following sections:
 - Section 4. Funding Level Update
 - Section 5. Investment Performance: A - Fund, B - Investment Managers
 - Section 7. Investment Strategy
 - Section 8. Portfolio Rebalancing and Cash Management
 - Section 9. Corporate Governance and Responsible Investment (RI) Update

2 RECOMMENDATION

The Avon Pension Fund Committee is asked to:

- 2.1 **Note the information set out in the report**
- 2.2 **Note LAPFF Quarterly Engagement Report at Appendix 4**

3 FINANCIAL IMPLICATIONS

3.1 The returns achieved by the Fund from 1 April 2013 will affect the next triennial valuation in 2016. Section 4 of this report discusses the trends in the Fund's liabilities and the funding level.

4 FUNDING LEVEL

4.1 Using information provided by the Actuary, Mercer has analysed the funding position as part of the report at Appendix 2 (section 2). This analysis shows the impact of both the assets and liabilities on the (estimated) funding level. ***It should be noted that this is just a snapshot of the funding level at a particular point in time.***

4.2 Key points from the analysis are:

- (1) The funding level has fallen 1% over the quarter from 78% to c. 77% and the deficit has risen slightly from c. £1.07bn to c. £1.1bn.
- (2) The deterioration over the quarter was largely due to negative asset returns over the quarter despite a rise in the discount rate from 3.9% to 4.3% reducing the value of liabilities.

5 INVESTMENT PERFORMANCE

A – Fund Performance

5.1 The Fund's assets decreased by £99m (a return of -2.6%) in the quarter, giving a value for the investment Fund of £3,730m at 30 June 2015. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers. Manager performance is monitored in detail by the Panel. The Fund's investment return and performance relative to benchmark is summarised below.

Table 1: Fund Investment Returns

Periods to 30 June 2015

	3 months	12 months	3 years (p.a.)
Avon Pension Fund (incl. currency hedging)	-2.6%	7.9%	10.9%
Avon Pension Fund (excl. currency hedging)	-3.0%	7.6%	10.5%
Strategic benchmark (no currency hedging)	-2.5%	8.1%	9.7%
<i>(Fund incl hedging, relative to benchmark)</i>	<i>(-0.1%)</i>	<i>(-0.2%)</i>	<i>(+1.2%)</i>
Local Authority Average Fund	-2.5%	8.2%	10.8%
<i>(Fund incl hedging, relative to benchmark)</i>	<i>(-0.1%)</i>	<i>(-0.3)</i>	<i>(+0.1%)</i>

5.2 **Fund Investment Return:** All Equity markets produced negative returns over the quarter in Sterling terms. Asia Pacific was the worst performing region (-8%) whilst the UK All Share Index fell by -1.6%. Bond yields rose sharply across all maturities leading to negative returns from Gilts (-6.3%) and Corporate Bonds (-3.9%).

5.3 Over 3 years all asset classes outperformed their strategic return assumption, with the exception of Emerging Market equities, hedge funds and overseas fixed interest.

5.4 **Fund Performance versus Benchmark: -0.2% over 12 months, attributed to**

- (1) **Asset Allocation:** The contribution to outperformance from asset allocation was **0.1%** over the 12 months. This was due to the underweights to Hedge Funds and Diversified Growth, and an overweight in developed overseas equities. The currency hedging programme contributed **0.3%** over 1 year.
- (2) **Manager Performance:** In aggregate, manager performance detracted **-0.6%** of the outperformance over the 12 month period, relative to the strategic benchmark, driven by under performance in overseas equities, hedge funds and property versus their individual benchmarks despite strong manager outperformance in UK equities.

5.5 **Versus Local Authority Average Fund:** Over one year, the Fund marginally underperformed the average fund.

5.6 **Currency Hedging:** The hedging programme is in place to manage the volatility arising from overseas currency exposure, in particular to protect the Fund as sterling strengthens and returns from foreign denominated assets reduce in sterling terms. The hedging programme has contributed +0.4% to the total Fund return over the quarter and added 0.3% over the year.

B – Investment Manager Performance

5.7 Eleven mandates met or exceeded their three year performance benchmark, which offset underperformance by Partners, Signet and Schroder Global Equity. SSgA, RLAM, and Jupiter all continue to perform particularly well against their three year performance targets.

5.8 Under the Red Amber Green (RAG) framework for monitoring manager performance, the Panel consider updates on all managers not currently achieving Green status including progress on action points. Any change in the RAG status of any manager is reported to Committee with an explanation of the change. **This quarter TT has been upgraded from Amber to a Green rating (explained in Exempt Appendix 3).** Currently 2 managers are amber rated, Schroder (global equity), and Signet (fund of hedge funds). It should be noted that the Fund has terminated its mandate with Signet.

6 INVESTMENT STRATEGY

6.1 Infrastructure: The Fund's investments in infrastructure are awaiting drawdown by the selected manager IFM who anticipate the funds being drawn down over the next 12 to 18 months.

6.2 The Investment Panel is undertaking a review of the Fund's management of liability risk which will form a significant part of the workplan over the coming months.

7 PORTFOLIO REBALANCING AND CASH MANAGEMENT

Portfolio Rebalancing

7.1 The rebalancing policy requires automatic rebalancing between the allocations to Liquid Growth (equities and diversified growth funds) and Stabilising (Bonds) assets when the liquid growth portion deviates from 75% by +/- 5%. Tactical rebalancing is allowed between deviations of +/- 2 to +/- 5%, on advice from the Investment Consultant. The implementation of this policy is delegated to Officers.

7.2 The Equity (inc. DGFs):Bond allocation is estimated to be 75.2: 24.8 at 26 August 2015 which is within the acceptable range, requiring no action.

Cash Management

- 7.3 Cash is held by the managers at their discretion within their investment guidelines, and internally to meet working requirements. The officers closely monitor the management of the Fund's cash held by the managers and custodian with a particular emphasis on the security of the cash.
- 7.4 Management of the cash held internally by the Fund to meet working requirements is delegated to the Council's Treasury Management Team. The monies are invested separately from the Council's monies.
- 7.5 The Fund continues to deposit internally managed cash on call with NatWest, Bank of Scotland and Svenska Handelsbanken. The Fund also deposits cash with the Goldman Sachs Asset Management Global Treasury Fund (AAA rated). Another AAA rated fund with Deutsche Bank is also available for deposits if required. The Fund also has access to the Government's Debt Management Office, however the interest paid currently may not cover the transfer and administration costs incurred.
- 7.6 During the period there were no breaches of the Fund's Treasury Management Policy (approved June 2015).
- 7.7 The 2015/16 Service Plan forecast an average cash outflow of c. £2m each month during the year to 31 March 2016. Unbudgeted inflows during the year including a deficit termination payment and expected reduced outflows have led to a revised cash flow forecast for the whole year of a £7m outflow.

8 CORPORATE GOVERNANCE UPDATE

- 8.1 During the quarter, the Fund's external managers undertook the following voting activity on behalf of the Fund:

Companies Meetings Voted:	578
Resolutions voted:	9,238
Votes For:	8,823
Votes Against:	380
Abstained:	54
Withheld* vote:	46

** A withheld vote is essentially the same as a vote to abstain, it reflects a view to vote neither for or against a resolution. Although the use of 'abstain' or 'withheld' reflects the different terms used in different jurisdictions, a 'withheld' vote can often be interpreted as a more explicit vote against management, where a minimum threshold of support is required.*

- 8.2 The Fund is a member of LAPFF, a collaborative body that exists to serve the investment interests of local authority pension funds. In particular, LAPFF seeks to maximise the influence the funds have as shareholders through co-ordinating shareholder activism amongst the pension funds. LAPFF's activity in the quarter is summarised in their quarterly engagement report at Appendix 4.

9 RISK MANAGEMENT

- 9.1 A key risk to the Fund is that the investments fail to generate the returns required to meet the Fund's future liabilities. This risk is managed via the Asset Liability Study which determines the appropriate risk adjusted return profile (or strategic benchmark) for the Fund and through the selection process followed before managers are appointed. This report monitors (i) the strategic policy and funding

level in terms of whether the strategy is on course to fund the pension liabilities as required by the funding plan and (ii) the performance of the investment managers. An Investment Panel has been established to consider in greater detail investment performance and related matters and report back to the committee on a regular basis.

10 EQUALITIES

10.1 An Equality Impact Assessment has not been completed as this report is for information only.

11 CONSULTATION

11.1 This report is for information and therefore consultation is not necessary.

12 ISSUES TO CONSIDER IN REACHING THE DECISION

12.1 The issues to consider are contained in the report.

13 ADVICE SOUGHT

13.1 The Council's Monitoring Officer (Divisional Director – Legal and Democratic Services) and Section 151 Officer (Divisional Director – Business Support) have had the opportunity to input to this report and have cleared it for publication.

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Background papers	LAPPF Member Bulletins, Data supplied by The WM Company
Please contact the report author if you need to access this report in an alternative format	