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Date: 18 February 2014
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**To: All Members of the Avon Pension Fund Committee - Investment Panel**

Councillor Charles Gerrish (Chair), Councillor Gabriel Batt, Ann Berresford, Councillor Mary Blatchford, Roger Broughton and Councillor Ian Gilchrist

Chief Executive and other appropriate officers
Press and Public

Dear Member

**Avon Pension Fund Committee - Investment Panel: Wednesday, 26th February, 2014**

You are invited to attend a meeting of the **Avon Pension Fund Committee - Investment Panel**, to be held on **Wednesday, 26th February, 2014** at **9.30 am** in the **Kaposvar Room - Guildhall, Bath.**

*Please note that following the formal meeting, there will be "Meet the Manager" presentations from Gottex and Signet in preparation for the review of hedge funds.*

The agenda is set out overleaf.

Yours sincerely

Sean O'Neill
for Chief Executive

**If you need to access this agenda or any of the supporting reports in an alternative accessible format please contact Democratic Services or the relevant report author whose details are listed at the end of each report.**

*This Agenda and all accompanying reports are printed on recycled paper*

**NOTES:**

1. **Inspection of Papers:** Any person wishing to inspect minutes, reports, or a list of the background papers relating to any item on this Agenda should contact Sean O'Neill who is available by telephoning Bath 01225 395090 or by calling at the Riverside Offices Keynsham (during normal office hours).

2. **Public Speaking at Meetings:** The Council has a scheme to encourage the public to make their views known at meetings. They may make a statement relevant to what the meeting has power to do. They may also present a petition or a deputation on behalf of a group. Advance notice is required not less than two full working days before the meeting (this means that for meetings held on Wednesdays notice must be received in Democratic Services by 4.30pm the previous Friday)

   The public may also ask a question to which a written answer will be given. Questions must be submitted in writing to Democratic Services at least two full working days in advance of the meeting (this means that for meetings held on Wednesdays, notice must be received in Democratic Services by 4.30pm the previous Friday). If an answer cannot be prepared in time for the meeting it will be sent out within five days afterwards. Further details of the scheme can be obtained by contacting Sean O'Neill as above.

3. **Details of Decisions taken at this meeting** can be found in the minutes which will be published as soon as possible after the meeting, and also circulated with the agenda for the next meeting. In the meantime details can be obtained by contacting Sean O'Neill as above.

   Appendices to reports are available for inspection as follows:-

   **Public Access points** - Riverside - Keynsham, Guildhall - Bath, Hollies - Midsomer Norton, and Bath Central, Keynsham and Midsomer Norton public libraries.

   **For Councillors and Officers** papers may be inspected via Political Group Research Assistants and Group Rooms/Members' Rooms.

4. **Attendance Register:** Members should sign the Register which will be circulated at the meeting.

5. THE APPENDED SUPPORTING DOCUMENTS ARE IDENTIFIED BY AGENDA ITEM NUMBER.

6. **Emergency Evacuation Procedure**

   When the continuous alarm sounds, you must evacuate the building by one of the designated exits and proceed to the named assembly point. The designated exits are sign-posted.

   Arrangements are in place for the safe evacuation of disabled people.

**Avon Pension Fund Committee - Investment Panel - Wednesday, 26th February, 2014**

**at 9.30 am in the Kaposvar Room - Guildhall, Bath**

**A G E N D A**

1. EMERGENCY EVACUATION PROCEDURE

   The Chair will draw attention to the emergency evacuation procedure as set out under Note 9.

2. DECLARATIONS OF INTEREST

   At this point in the meeting declarations of interest are received from Members in any of the agenda items under consideration at the meeting. Members are asked to complete the green interest forms circulated to groups in their pre-meetings (which will be announced at the Council Meeting) to indicate:

   (a) The agenda item number in which they have an interest to declare.

   (b) The nature of their interest.

   (c) Whether their interest is a **disclosable pecuniary interest** or an **other interest**, (as defined in Part 2, A and B of the Code of Conduct and Rules for Registration of Interests)

   Any Member who needs to clarify any matters relating to the declaration of interests is recommended to seek advice from the Council's Monitoring Officer or a member of his staff before the meeting to expedite dealing with the item during the meeting.

3. APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

   To receive any declarations from Members of the Committee and Officers of personal/prejudicial interests in respect of matters for consideration at this meeting, together with their statements on the nature of any such interest declared.

4. TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

5. ITEMS FROM THE PUBLIC - TO RECEIVE DEPUTATIONS, STATEMENTS, PETITIONS OR QUESTIONS

6. ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

   To deal with any petitions or questions from Councillors and, where appropriate, co-opted and added members.

7. MINUTES: 15 NOVEMBER 2013 (Pages 7 - 14)

8. REVIEW OF INVESTMENT PERFORMANCE FOR PERIODS ENDING 31 DEC 2013 (Pages 15 - 78)

   *Before discussing appendices 3 and 4 of this item, Members are invited to consider*

*the arguments set out in the Public Interest document and to pass the following resolution:*
*"That the Committee having been satisfied that the public interest would be better served by not disclosing relevant information, the public shall be excluded from the meeting for the duration of the discussion of exempt appendices, 3 and 4 of this item, in accordance with the provisions of section 100(A)(4) of the Local Government Act 1972, because of the likely disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Act as amended."*

9. INFRASTRUCTURE TENDER PROCESS (Pages 79 - 86)

10. HEDGE FUND REVIEW - SCOPE (Pages 87 - 90)

11. WORKPLAN (Pages 91 - 94)

The Committee Administrator for this meeting is Sean O'Neill who can be contacted on 01225 395090.

# Protocol for Decision-making

## Guidance for Members when making decisions

When making decisions, the Cabinet/Committee must ensure it has regard only to relevant considerations and disregards those that are not material.

The Cabinet/Committee must ensure that it bears in mind the following legal duties when making its decisions:

- Equalities considerations
- Risk Management considerations
- Crime and Disorder considerations
- Sustainability considerations
- Natural Environment considerations
- Planning Act 2008 considerations
- Human Rights Act 1998 considerations
- Children Act 2004 considerations
- Public Health & Inequalities considerations

Whilst it is the responsibility of the report author and the Council's Monitoring Officer and Chief Financial Officer to assess the applicability of the legal requirements, decision makers should ensure they are satisfied that the information presented to them is consistent with and takes due regard of them.

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**Bath and North East Somerset Council**

**AVON PENSION FUND COMMITTEE - INVESTMENT PANEL**

# Minutes of the Meeting held

Friday, 15th November, 2013, 2.00 pm

**Members:** Councillor Charles Gerrish (Chair), Councillor Mary Blatchford and Councillor Ian Gilchrist
**Advisors:** Tony Earnshaw (Independent Advisor)
**Also in attendance:** Tony Bartlett (Head of Business, Finance and Pensions), Liz Woodyard (Investments Manager), Matt Betts (Assistant Investments Manager) and Matthew Clapton (Investments Officer)

## 34 EMERGENCY EVACUATION PROCEDURE

The Democratic Services Officer read out the procedure.

## 35 DECLARATIONS OF INTEREST

There were none.

## 36 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

Apologies were received from Cllr Gabriel Batt and Roger Broughton.

## 37 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

## 38 ITEMS FROM THE PUBLIC - TO RECEIVE DEPUTATIONS, STATEMENTS, PETITIONS OR QUESTIONS

There was none.

## 39 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

## 40 MINUTES: 4TH SEPTEMBER 2013

The public and exempt minutes of the meeting of 4th September 2013 were approved as a correct record and signed by the Chair.

## 41 REVIEW OF INVESTMENT PERFORMANCE FOR PERIODS ENDING 30 SEPTEMBER 2013

The Assistant Investments Manager presented the report. He said that the Fund had increased by 2.3% over the quarter and had outperformed the strategic benchmark over the quarter and the year. Of the 5 managers rated as Amber in the RAG report (Exempt Appendix 3) 3 had continued to improve, while 2 had deteriorated. He drew attention to the update on the implementation of the investment strategy contained in section 4 of the report. Rebalancing had taken place in the quarter, and overweight equity had been reduced and the proceeds reinvested in corporate bonds.

A Member questioned the statement in paragraph 3.8 at the bottom of agenda page 14 that the issue of the Fund being practically the only investor in the SSgA European fund “was last addressed by the Panel in November 2011”, whereas in fact it had appeared regularly on agendas. The Investments Manager replied that it was not a new issue, though it had been monitored constantly. The Chair agreed with the Member that the issue had been constantly before the Committee.

Mr Finch and Mr Sheth commented on the JLT investment report. Mr Finch noted that MAN was struggling, vindicating the Committee’s decision to disinvest from them, even though JLT had advised at the time holding and watching them a little longer. He said that there were very few negatives over the quarter, apart from emerging markets. Overall managers were doing pretty much what the Fund wanted them to do. Mr Sheth commented on the performance of individual managers.

The Chair asked about the impact of the fall in the dollar. Mr Sheth said that it made some countries’ exports less competitive. Mr Finch, however, said that it had to be remembered that in Asian countries a high proportion of the population was under 25: growth in domestic demand could offset poorer export performance.

A Member noted that Blackrock appeared in the middle of the charts, which seemed natural enough since almost half the Fund was invested in them. Mr Finch said that was how Blackrock was intended to perform and they were performing their expected role. The Blackrock portfolio comprised long-term assets which were fairly static. The Member asked whether it was typical for a local authority pension fund to have this type of dominant portfolio. The investments manager replied that most, but not all, funds had a large passive fund, which helped manage overall investment costs.

The Independent Adviser suggested that the structure of reports should reflect the new investment structure of the Fund. Mr Finch agreed that this was a good idea.

Before discussing the exempt appendices, the Committee **RESOLVED**

> “that having been satisfied that the public interest would be better served by not disclosing relevant information, the public shall be excluded from the meeting for the duration of the discussion of exempt appendices, 3, 4 and 5 of this item, in accordance with the provisions of section 100(A)(4) of the Local Government Act 1972, because of the likely disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Act as amended.”

**RESOLVED** to note the information as set out in the report.

## 42 INFRASTRUCTURE

The Investments Manager presented the report. The Panel was being invited to approve the proposed policy framework. She reminded Members that it had been agreed to take the issue to the full Committee, because Infrastructure would constitute a new asset class. Mr Finch would lead a briefing session before the

December meeting of the Committee. There were many different ways of investing in infrastructure, so it was proposed to delegate as much of the detailed decision making to officers and the Panel as possible. If the framework was too prescriptive it would prevent the Fund from taking advantage of available opportunities. Infrastructure was not like the Diversified Growth Fund or Emerging Markets where a fairly tight specification could be drawn up in advance. Mr Finch agreed that infrastructure was a broad category with many access routes. What was the point of having an infrastructure asset class? The answer was to take advantage of its different behaviour, which would provide additional diversification and an ongoing income stream.

The Chair said that there a number of issues to be considered. One was whether to invest in listed or unlisted companies. The other was UK versus global. There seemed to be far greater infrastructure opportunities outside the UK. A Member noted that one of the things the Fund was looking for was inflation protection, which might be easier to secure from UK rather than global assets. The Chair said that a third issue was whether infrastructure investment should be done directly in individual projects, or through a fund of funds structure. The Investments Manager said this would not be specified in advance; a tender would be issued and submissions reviewed. Mr Finch said that a important factor would be when funds were closed; the aim was to get projects going and to start earning returns as soon as possible.

A Member asked about the tender process to be followed. The Investments Manager replied that a significant issue was whether to go through the Official Journal of the European Union (OJEU) process or not. The OJEU process imposed a number of restrictions, such as not be able to respecify at a later stage. The Member said that an issue she would be concerned about would be the level of debt in particular projects. The Assistant Investments Manager suggested that leverage was part of every project. The Member, however, thought that the protection against interest rate changes was required.

A Member raised the possibility of reputational risk, for example through investments that harmed the environment. The Investments Manager responded that once a manager had been appointed, it would not be possible to control what they invested in. The Committee could only exercise control at the tender stage and through the due diligence process. The Head of Business, Finance and Pensions suggested that environmental regulation was so strict that there was little to fear, but the Member felt that this did not apply in emerging markets. The Investments Manager responded that the Fund did not need to invest in infrastructure in emerging markets to achieve its objectives. She suggested that there could be a discussion at the February Committee meeting on how to weight different aspects in the tender evaluation process.

A Member noted that a pension fund was a major investor in the Bath casino project. The Investments Manager replied that the Fund would only be able to invest directly in a limited number of projects, and so would not get the diversification that was desired by the direct investment route. Skilled investment managers were also required to achieve the best returns.

The Chair wondered whether having an investment partnership with other pension funds would give extra bargaining power. Mr Finch suggested that a company could be created as a joint investment vehicle. Alternatively agreement could be reached about data sharing, so that data gathering would only have to be done once by one of the partner funds.

The Chair wondered how the rate of return should be specified, as a percentage or linked to inflation. Mr Sheth said that it could be specified in a number of ways.

At the conclusion of the discussion, it was **RESOLVED**

1. to recommend that proposed policy framework as amended should be presented to the Committee for approval at the December 2013 committee meeting;

2. To delegate the tender process to officers who will consult the panel as required.

## 43 WORKPLAN

**RESOLVED** to note the workplan.

The Assistant Investments Manager asked Members to note that, since it had been agreed to meet each of the Fund's managers every two years, it would be necessary to have more workshops either immediately before or after meetings.

The meeting ended at 3.52 pm

Chair(person) ..........................................................................................

Date Confirmed and Signed ..................................................................

**Prepared by Democratic Services**

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Document is Restricted

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| Bath & North East Somerset Council | | |
|---|---|---|
| MEETING: | **AVON PENSION FUND INVESTMENT PANEL** | |
| MEETING DATE: | **26 FEBRUARY 2014** | AGENDA ITEM NUMBER **8** |
| TITLE: | **Review Of Investment Performance For Periods Ending 31 Dec 2013** | |
| WARD: | **ALL** | |
| **AN OPEN PUBLIC ITEM** | | |
| List of attachments to this report:<br>Appendix 1 – Fund Valuation<br>Appendix 2 – JLT performance monitoring report (shortened version)<br>**Exempt** Appendix 3 – RAG Monitoring Summary Report<br>**Exempt** Appendix 4 – Emerging Markets Equity Fund Update | | |

## 1 THE ISSUE

1.1 This paper reports on the performance of the Fund's investment managers and seeks to update the Panel on routine aspects of the Fund's investments. The report contains performance statistics for periods ending 31 December 2013.

1.2 The report focuses on the performance of the individual investment managers. The full performance report with aggregate investment and funding analysis will be reported to the Committee meeting on 28 March 2014.

## 2 RECOMMENDATION

**That the Investment Panel:**

2.1 **Notes the information as set out in the report.**

2.2 **Identifies any issues to be notified to the Committee.**

## FINANCIAL IMPLICATIONS

2.3 The returns achieved by the Fund for the three years commencing 1 April 2013 will impact the next triennial valuation which will be calculated as at 31 March 2016.

## 3 INVESTMENT PERFORMANCE

### A – Fund Performance

3.1 The Fund's assets increased by £129m (c. 4%) in the quarter, giving a value for the investment Fund of £3,299m at 31 December 2013. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers.

3.2 The majority of equity markets were positive over the quarter led by the US and other western developed markets, whilst Asian markets were relatively flat. The exception was emerging markets equities which experienced a small fall. In contrast, gilts and corporate bonds produced small negative returns as bond yields rose over the quarter.

3.3 The Fund's overall performance relative to benchmarks is unavailable at the time of publishing. Full performance data will be reported to the Pensions Committee on 28 March 2014.

### B – Investment Manager Performance

3.4 A detailed report on the performance of each investment manager has been produced by JLT – see pages 15 to 35 of Appendix 2.

3.5 The Fund invested in two new Diversified Growth managers during the quarter, Barings and Pyrford, and was fully invested by the end of November. They will be included in JLT's performance report at Appendix 2 from next quarter.

3.6 Schroder global equity presented to the Panel in Nov 2013 following departure of the fund manager. The Panel were reassured that the recent changes should bring about improved performance for the mandate but wished to continue monitoring the portfolio closely to ensure the team changes are managed well. A +0.9% outperformance of the index this quarter has resulted in Schroder's outperformance against their 1 year target improving (1.7% outperformance versus 2% p.a. target).

3.7 Jupiter, Invesco, Genesis, SSgA, RLAM, Schroders Property and Partners are all outperforming their three year performance targets.

3.8 State Street UK has been fined £23m by the Financial Conduct Authority (FCA) for failings in their transitions management business. This is a separate business from their asset management business State Street Global Advisors (SSgA) who manage 2 mandates on behalf of the Fund. The service the Fund received was in no way affected by the failings in the transition management business.

3.9 Exempt Appendix 3 summarises the latest Performance Monitoring Report used internally to monitor manager performance. The summary report highlights the managers that are rated Amber or Red, detailing the performance and/or organisational issue(s), how they are being monitored and any actions taken by officers and/or the Panel.

3.10 The RAG report at Exempt Appendix 3 highlights the following corporate changes since the last meeting:

(1) In December Gottex announced a merger with EIM (a $3bn FoHF manager with relatively similar business with similar global footprint). The rationale is to achieve cost efficiencies and scale by merging 2 similar businesses. Gottex will present to the Panel in a Workshop following the formal meeting.

## 4 INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

4.1 Changes to the Investment Strategy agreed in March 2013 are in the process of being implemented and progress is as follows:

| | Project | Progress |
|---|---|---|
| 1 | DGF Mandates | Complete:<br>Investments made during the quarter. Focus is now on setting up reporting and monitoring. |
| 2 | Emerging Market Equity Mandate | Complete:<br>Selection decision made w/c 2 December 2013. See Exempt Appendix 4. Investments made in January 2014. Focus is now on setting up reporting and monitoring. |
| 3 | Restructuring passive equity portfolio | Complete:<br>Converted to income distributing funds for a number of the passive equity funds managed by BlackRock. |
| 4 | Rebalancing bond portfolio | Complete:<br>Strategic allocation between UK gilts and corporate bonds implemented 16 August |
| 5 | Infrastructure | On Track:<br>Paper with update on tender process for discussion at this meeting. |

4.2 Following the rebalancing undertaken in October 2013 to reduce the overweight to equities (as the allocation was approaching the automatic trigger point for rebalancing), there has been no further rebalancing. The latest Equity:Bond allocation is 77.7 : 22.3 as at 5 February 2014. This remains within the tactical range for rebalancing. Officers will continue to incorporate any rebalancing considerations as the new strategy is implemented.

## 5 RISK MANAGEMENT

5.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. 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 the performance of the investment managers. The 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.

## 6 EQUALITIES

6.1 An equalities impact assessment is not necessary as the report is primarily for information only.

## 7 CONSULTATION

7.1 This report is primarily for information and therefore consultation is not necessary.

## 8 ISSUES TO CONSIDER IN REACHING THE DECISION

8.1 The issues to consider are contained in the report.

## 9 ADVICE SOUGHT

9.1 The Council's Monitoring Officer (Divisional Director – Legal & 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.

| | |
|---|---|
| **Contact person** | Matt Betts, Assistant Investments Manager (Tel: 01225 395420) |
| **Background papers** | Data supplied by The WM Company |
| **Please contact the report author if you need to access this report in an alternative format** | |

**AVON PENSION FUND VALUATION – 31 DECEMBER 2013**

| | Passive Multi-Asset | | Active Equities | | | | Enhanced Indexation | | Active Bonds | Funds of Hedge Funds | DGFs | Property | In House Cash/ | TOTAL | Avon Asset Mix % |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| All figures in £m | Black-Rock | Black-Rock 2* | TT Int'l | Jupiter (SRI) | Genesis | Schroder Global | Invesco | SSgA | RLAM | | Barings/ Pyrford | Schroder/ Partners | Currency Hedging | | |
| **EQUITIES** | | | | | | | | | | | | | | | |
| UK | 299.4 | 12.9 | 183.9 | 154.1 | | 23.1 | | | | | | | | 673.5 | 20.41% |
| North America | 171.1 | 5.9 | | | | 120.1 | | | | | | | | 297.1 | 9.01% |
| Europe | 154.6 | | | | | 29.7 | | 39.9 | | | | | | 224.1 | 6.79% |
| Japan | 42.5 | | | | | 14.9 | | 38.2 | | | | | | 95.6 | 2.90% |
| Pacific Rim | 52.3 | | | | | 9.7 | | 29.7 | | | | | | 91.7 | 2.78% |
| Emerging Mkts | | | | | 145.7 | 14.0 | | | | | | | | 159.7 | 4.84% |
| Global ex-UK | | | | | | | 236.6 | | | | | | | 236.6 | 7.17% |
| Global inc-UK | 79.9 | | | | | | | | | | | | 9.1 | 89.0 | 2.70% |
| ***Total Overseas*** | ***500.4*** | ***5.9*** | | | ***145.7*** | ***188.4*** | ***236.6*** | ***107.8*** | | | | | ***9.1*** | ***1193.9*** | ***36.19%*** |
| **Total Equities** | **799.8** | **18.8** | **183.9** | **154.1** | **145.7** | **211.4** | **236.6** | **107.8** | | | | | **9.1** | **1867.3** | **56.61%** |
| **DGFs** | | | | | | | | | | | **315.2** | | | **315.2** | |
| **BONDS** | | | | | | | | | | | | | | | |
| I/L Gilts | 183.9 | | | | | | | | | | | | | 183.9 | 5.57% |
| Conv Gilts | 91.1 | 13.8 | | | | | | | | | | | | 104.9 | 3.18% |
| Corporate Bds | 17.7 | | | | | | | | 242.1 | | | | | 259.9 | 7.88% |
| Overseas Bds | 73.1 | | | | | | | | | | | | | 73.1 | 2.22% |
| **Total Bonds** | **365.8** | **13.8** | | | | | | | **242.1** | | | | | **621.7** | **18.85%** |
| Hedge Funds | | | | | | | | | | 162.7 | | | | 162.7 | 4.93% |
| Property | | | | | | | | | | | | 250.9 | | 250.9 | 7.60% |
| Cash | 5.0 | 13.4 | 1.8 | 9.5 | | 4.0 | | | | | | 1.2 | 46.2 | 81.0 | 2.46% |
| **TOTAL** | **1170.6** | **45.9** | **185.7** | **163.6** | **145.7** | **215.4** | **236.6** | **107.8** | **242.1** | **162.7** | **315.2** | **252.1** | **55.3** | **3298.8** | **100.0%** |

N.B. (i) Valued at BID (where appropriate)
(ii) In-house cash = short term deposits at NatWest managed on our behalf by B&NES plus general cash held at Custodian
(iii) BlackRock 2 * = represents the assets to be invested in property, temporarily managed by BlackRock

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# Avon Pension Fund

Review for period to 31 December 2013

# Contents

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# 1 Executive Summary

This report is produced by JLT Employee Benefits ("JLT") to assess the performance and risks of the investment managers of the Avon Pension Fund (the "Fund"), and of the Fund as a whole.

This version of the report has been prepared for the Investment Panel, based on initial manager data. A full version of this report will be reported to the full Committee meeting once the final WM data has been received.

### Fund performance

- The value of the Fund's assets increased by £129m over the fourth quarter of 2013 to £3,299m.

### Strategy

- Equity markets were generally positive over the last quarter. The highest returns were from the USA (+7.9%) with other Western developed markets returning around 5%. Emerging market equities fell by 0.7%, whereas Japanese and Asia Pacific equities returned 0.1% and 0.0% respectively.
- The USA was also the best performer in equity markets over the last twelve months, at 30.4%. UK, European and Japanese equities all produced returns in excess of 20%. Emerging market equities (-5.3%) and Asia Pacific (1.3%) lagged.
- The three year developed market equity returns remained ahead of the assumed strategic return but the emerging market equity return is significantly behind its assumed strategic return over 3 years.
- Gilt and corporate bond markets produced small negative returns as bond yields rose. Over the three year period returns remain ahead of the assumed strategic return as poor 2010 returns fell out of the rolling three year period.
- The Overseas Fixed Interest return has fallen to -0.7% p.a. over three years. This has been affected by rising yields within European bonds, and more recently by healthy US economic data and the announcement that the US Federal Reserve would start to scale back its asset purchase programme.
- Hedge funds remain below the assumed strategic returns but the Property return is now just ahead as returns improve.

### Managers

- Returns from all managers were positive in absolute terms over the last quarter, with the exception of Genesis (-0.3%) and SSgA Pacific (-0.2%). The best performing funds were the UK equity funds, TT (8.8%) and Jupiter (7.6%).
- The highest one-year returns also came from the UK equity managers, with Jupiter at 31.0% and TT at 28.3%.
- Over three years, SSgA Pacific and Genesis were affected by relatively poor returns in Asia and the emerging markets. SSgA Pacific's return has fallen from 8.1% p.a. to 4.3% p.a. and Genesis' return has fallen from 1.8% p.a. to -0.9% p.a. This is due to market returns and both managers have actually outperformed their benchmarks over this period, meeting their objectives.
- TT outperformed over three years but did not meet their three-year target.

- The only other managers to not meet their three-year target were the hedge fund managers, who each produced negative relative returns over 3 years, but Stenham and Gottex both outperforming 1 year targets.
- Both the SSgA Europe ex UK and Pacific incl Japan enhanced equity pooled funds remain at a size such that Avon's investment now represents almost all of the pooled fund holdings. However, the Panel has previously concluded that the funds could be sustained even if the Avon Pension Fund was the only investor.

## Key points for consideration

- Emerging market equities could continue to suffer negative sentiment as growth rates slow and the US tapers its asset purchase programme.
  - Most commentators suggest weak returns are due to negative sentiment rather than fundamental structural concerns;
  - With the recent increase in the strategic allocation to this area, the Panel should consider these factors in the context of the long-term outlook for outperformance versus developed markets despite short term sentiment and volatility.
- Whilst it is too short a period to draw any concrete conclusions, there does not appear to have been any immediate negative impact on the performance of the Schroder Global Equity Portfolio following the departure of Virginie Maisonneuve.
- In January 2014, State Street were fined £22.9m by the FCA for overcharging six clients that used its transition management service between June 2010 and September 2011. We note that this was a different part of the business to their fund management and does not affect the funds.

# 2 Market Background

The figures below cover the three months, 1 year and 3 years to the end of December 2013.

## Market Statistics

| Yields as at 31 December 2013 | % p.a. |
|---|---|
| UK Equities | 3.28 |
| UK Gilts (>15 yrs) | 3.58 |
| Real Yield (>5 yrs ILG) | 0.03 |
| Corporate Bonds (>15 yrs AA) | 4.42 |
| Non-Gilts (>15 yrs) | 4.63 |

| Absolute Change in Yields | 3 Mths % | 1 Year % | 3 Years % |
|---|---|---|---|
| UK Equities | -0.13 | -0.29 | 0.39 |
| UK Gilts (>15 yrs) | 0.17 | 0.58 | -0.56 |
| Index-Linked Gilts (>5 yrs) | 0.07 | 0.10 | -0.46 |
| Corporate Bonds (>15 yrs AA) | 0.11 | 0.35 | -1.00 |
| Non-Gilts (>15 yrs) | 0.12 | 0.41 | -0.77 |

| Market Returns Bond Assets | 3 Mths % | 1 Year % | 3 Years % p.a. |
|---|---|---|---|
| UK Gilts (>15 yrs) | -1.8 | -5.9 | 6.9 |
| Index-Linked Gilts (>5 yrs) | -0.9 | 0.6 | 7.6 |
| Corporate Bonds (>15 yrs AA) | -0.3 | 0.0 | 7.8 |
| Non-Gilts (>15 yrs) | -0.3 | -0.6 | 8.0 |

| Market Returns Growth Assets | 3 Mths % | 1 Year % | 3 Years % p.a. |
|---|---|---|---|
| UK Equities | 5.5 | 20.8 | 9.4 |
| Overseas Equities | 5.0 | 21.2 | 8.1 |
| USA | 7.9 | 30.4 | 14.1 |
| Europe | 5.2 | 24.0 | 7.4 |
| Japan | 0.1 | 25.0 | 4.0 |
| Asia Pacific (ex Japan) | 0.0 | 1.3 | 0.5 |
| Emerging Markets | -0.7 | -5.3 | -4.5 |
| Property | 4.7 | 10.9 | 7.1 |
| Hedge Funds | 4.2 | 10.0 | 5.2 |
| Commodities | -2.5 | -3.1 | -2.6 |
| High Yield | 1.5 | 6.0 | 7.7 |
| Emerging Market Debt | 1.5 | -5.3 | 6.1 |
| Senior Secured Loans | 2.2 | 9.2 | 6.3 |
| Cash | 0.1 | 0.4 | 0.5 |

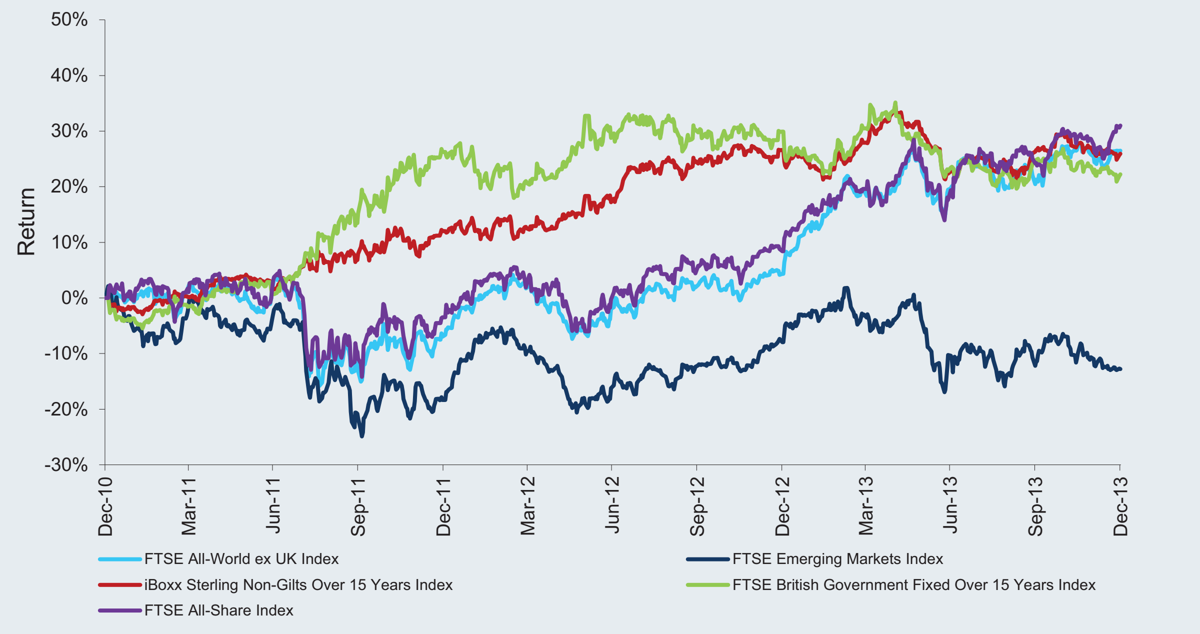
| Change in Sterling | 3 Mths % | 1 Year % | 3 Years % p.a. |
|---|---|---|---|
| Against US Dollar | 2.3 | 1.9 | 1.9 |
| Against Euro | 0.5 | -2.5 | 1.0 |
| Against Yen | 9.6 | 23.9 | 11.1 |

| Inflation Indices | 3 Mths % | 1 Year % | 3 Years % p.a. |
|---|---|---|---|
| Price Inflation – RPI | 0.6 | 2.7 | 3.5 |
| Price Inflation – CPI | 0.5 | 2.0 | 3.0 |
| Earnings Inflation * | -0.1 | 0.8 | 1.4 |

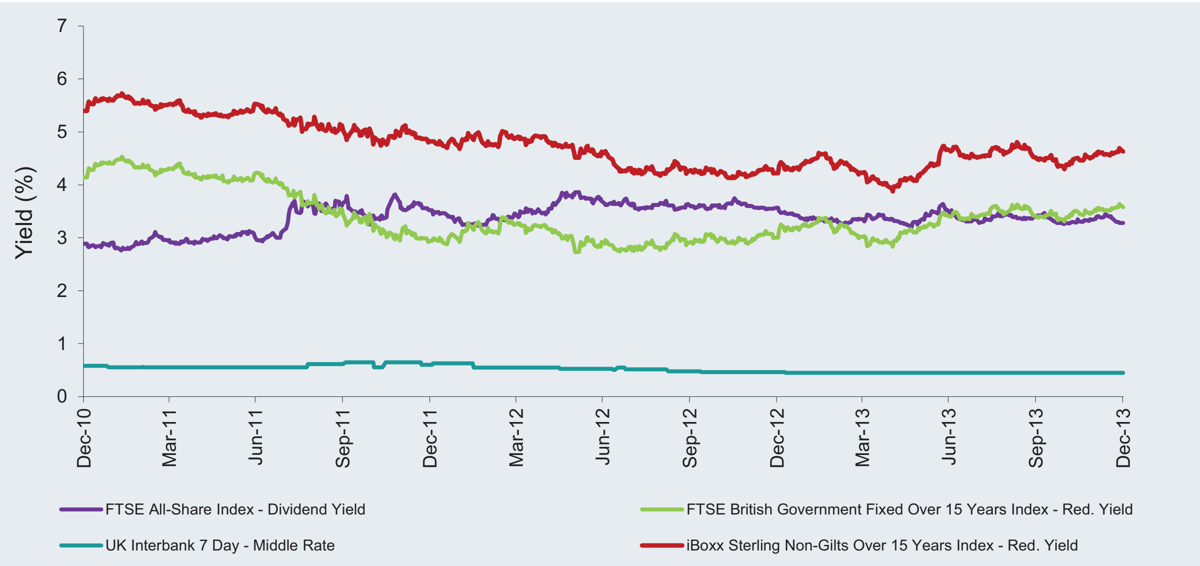
* Subject to 1 month lag

Source: Thomson Reuters and Bloomberg

## Market Summary charts




The graph above shows market returns for the last three years; both the medium-term trend and the short-term volatility.




The trend over the last 3 years until the end of April 2013 shows falling UK gilts and corporate bond yields, whilst the dividend yield on the FTSE All-Share Index has risen. Bond yields have increased slightly in the last 8 months whilst the dividend yield has remained relatively flat.

The table below compares general market returns (i.e. not achieved Fund returns) to 31 December 2013, with assumptions about returns made in the Investment Strategy agreed in 2013.

| Asset Class | Strategy Assumed Return % p.a. | 3 year Index Return % p.a. | Comment |
|---|---|---|---|
| Developed Equities | 8.25 | 8.8 | Ahead of the assumed strategic return following strong returns throughout the period apart from mid-2011. This quarter, markets have continued to rise although not as strongly as in Q4 2010 (which has fallen out of the 3-year return), hence returns are lower than in the last report. |
| Emerging Market Equities | 8.75 | -4.5 | In contrast to long term performance, the 3-year return from emerging market equities has fallen significantly due to negative sentiment from slowing growth and the withdrawal of capital as the US begins to taper its asset purchase programme. |
| UK Gilts | 4.5 | 6.9 | Ahead of the assumed strategic return as gilt yields fell significantly during 2011 and have fallen in the last quarter. Index-linked returns fell over the last quarter as UK inflation continued to decline. |
| Index Linked Gilts | 4.25 | 7.6 | |
| UK Corporate Bonds | 5.5 | 6.8 | |
| Overseas Fixed Interest | 5.5 | -0.7 | Behind the assumed strategic return, falling to a negative absolute return. In the last quarter, healthy US economic data and speculation over when the Federal Reserve would scale back its asset purchase programme put upward pressure on US bond yields. "Core" European bonds followed the US lead, whilst Europe's peripheral markets (Italy, Spain, Portugal, Ireland and Greece) delivered good quarterly performance but their three year returns were still affected by rising yields. |
| Fund of Hedge Funds | 6.0 | 2.7 | Behind the assumed strategic return following a negative return in 2011. More recently returns have been improving, with the return over the last twelve months being 7.7%. |
| Property | 7.0 | 7.1 | This is now slightly ahead of the assumed strategic return and continues to improve as property prices begin to rise. |

Source: Statement of Investment Principles, Thomson Reuters.

See appendix A for economic data and commentary.

# 3 Fund Valuations

The table below shows the asset allocation of the Fund as at 31 December 2013, with the BlackRock Multi-Asset portfolio and the BlackRock property portfolio (assets "ring fenced" for investment in property) split between the relevant asset classes.

| Asset Class | 31 December 2013 Value £'000 | Proportion of Total % | Strategic Benchmark Weight % |
|---|---|---|---|
| Developed Market Equities | 1,721,609 | 52.2 | 40.0 |
| Emerging Market Equities | 145,731 | 4.4 | 10.0 |
| Diversified Growth Funds (DGF) | 315,186 | 9.6 | 10.0 |
| Bonds | 621,730 | 18.8 | 20.0 |
| Fund of Hedge Funds | 162,737 | 4.9 | 5.0 |
| Infrastructure | - | - | 5.0 |
| Cash (including currency instruments) | 81,021 | 2.5 | - |
| Property | 250,853 | 7.6 | 10.0 |
| | | | |
| **TOTAL FUND VALUE** | **3,298,868** | **100.0** | **100.0** |

Source: Data provided by WM Performance Services

- The value of the Fund's assets increased by £129m over the fourth quarter of 2013 to £3,299m. Approximately £315m was invested into DGF.
- In terms of the asset allocation, the move from Man and Blackrock into Pyford, Barings and RLAM has reduced the developed market equity allocation and hedge fund allocation and introduced DGFs.
- Deviations from the strategic benchmark weight will continue during the period that changes to the investment strategy, agreed in 2013, are implemented. The overweight position to developed market equities relative to emerging market equities is expected to be reduced during Q1 2014.
- An allocation to infrastructure is expected to be built up over time.

| Manager | Asset Class | 30 September 2013 Value £'000 | 30 September 2013 Proportion of Total % | Net new money £'000 | 31 December 2013 Value £'000 | 31 December 2013 Proportion of Total % |
|---|---|---|---|---|---|---|
| Jupiter | UK Equities | 151,976 | 4.8 | - | 163,577 | 5.0 |
| TT International | UK Equities | 171,207 | 5.4 | - | 185,688 | 5.6 |
| Invesco | Global ex-UK Equities | 223,388 | 7.0 | - | 236,622 | 7.2 |
| Schroder | Global Equities | 203,330 | 6.4 | - | 215,489 | 6.5 |
| SSgA | Europe ex-UK Equities and Pacific incl. Japan Equities | 105,517 | 3.3 | - | 107,799 | 3.3 |
| Genesis | Emerging Market Equities | 146,181 | 4.6 | - | 145,731 | 4.4 |
| MAN | Fund of Hedge Funds | 63,607 | 2.0 | -61,898 | 1,651 | 0.1 |
| Signet | Fund of Hedge Funds | 65,903 | 2.1 | - | 66,477 | 2.0 |
| Stenham | Fund of Hedge Funds | 35,966 | 1.1 | - | 37,657 | 1.1 |
| Gottex | Fund of Hedge Funds | 55,755 | 1.8 | - | 56,953 | 1.7 |
| BlackRock | Passive Multi-asset | 1,430,170 | 45.2 | -307,013 | 1,170,637 | 35.5 |
| BlackRock (property fund) | Equities, Futures, Bonds, Cash (held for property inv) | 51,032 | 1.6 | -6,300 | 45,915 | 1.4 |
| RLAM | Bonds | 196,005 | 6.2 | 45,000 | 242,148 | 7.3 |
| Schroder | UK Property | 139,246 | 4.4 | - | 146,148 | 4.4 |
| Partners | Property | 97,169 | 3.1 | 6,800 | 105,871 | 3.2 |
| Record Currency Mgmt | Dynamic Currency Hedging | 7,877 | 0.2 | - | 21,421 | 0.6 |
| Record Currency Mgmt 2 | Overseas Equities (to fund currency hedge) | 7,426 | 0.2 | - | 9,092 | 0.3 |
| Pyrford | DGF | - | - | 105,000 | 104,320 | 3.2 |
| Barings | DGF | - | - | 210,000 | 210,866 | 6.4 |
| Internal Cash | Cash | 17,970 | 0.6 | 8,411 | 24,807 | 0.8 |
| Rounding | | - | - | - | -1 | - |
| **TOTAL** | | **3,169,725** | **100.0** | **0** | **3,298,868** | **100.0** |

Source: Avon Pension Fund Data provided by WM Performance Services

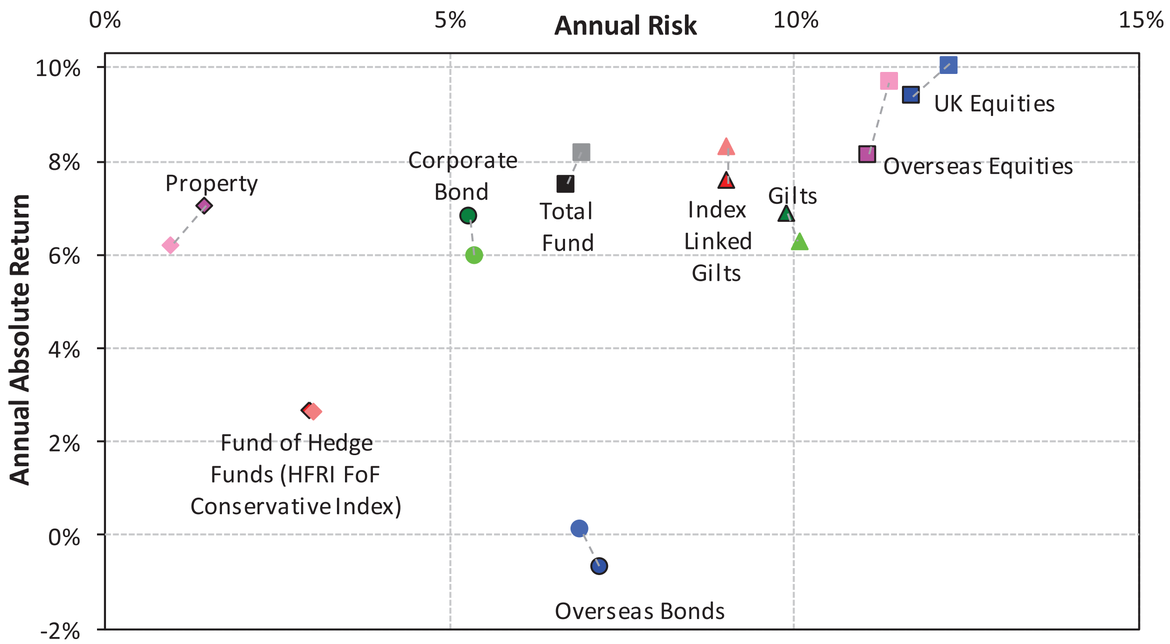
# 4 Performance Summary

## Risk Return Analysis

The chart below shows the 3 year absolute return ("Annual Absolute Return") against the 3 year volatility of absolute returns ("Annual Risk"), based on monthly/quarterly (as available) data points in sterling terms, to the end of December 2013 of each of the underlying asset benchmarks, along with the total Fund strategic benchmark. We also show the position as at last quarter, as shadow points.

This chart can be compared to the 3 year risk vs return managers' chart on page 13.

**3 Year Risk v 3 Year Return to 31 December 2013**

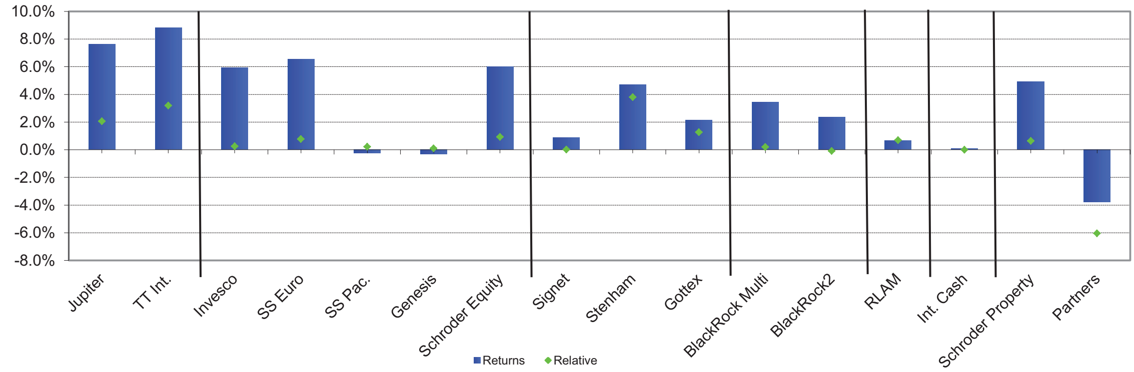



- All of the underlying benchmarks except overseas bonds have produced a positive return over the period (3 years p.a.).
- The three year return has decreased for both UK and overseas equities but increased for gilts and corporate bonds. Equities produced positive returns over the final quarter of 2013, but the higher returns of Q4 2010 have fallen out of the analysis. Conversely, bonds fell in the final quarter of 2013 as yields rose, but there were larger falls in Q4 2010.
- Equities remain the best performing asset class over three years, followed by index-linked gilts, property and conventional gilts.
- The property return continues to increase.
- The hedge funds index continues to produce steady returns, with very little change in the rolling 3 year return.
- Overseas bonds moved to a negative 3 year absolute return as US bond yields rose.
- In terms of risk, the three-year volatility has decreased slightly for each of the asset classes apart from property and overseas bonds.
- The three-year return on UK equities, gilts, index-linked gilts and corporate bonds remain above their assumed strategic return. Overseas bonds and hedge funds remain below their assumed strategic return, whist property is now marginally ahead of its assumed strategic return

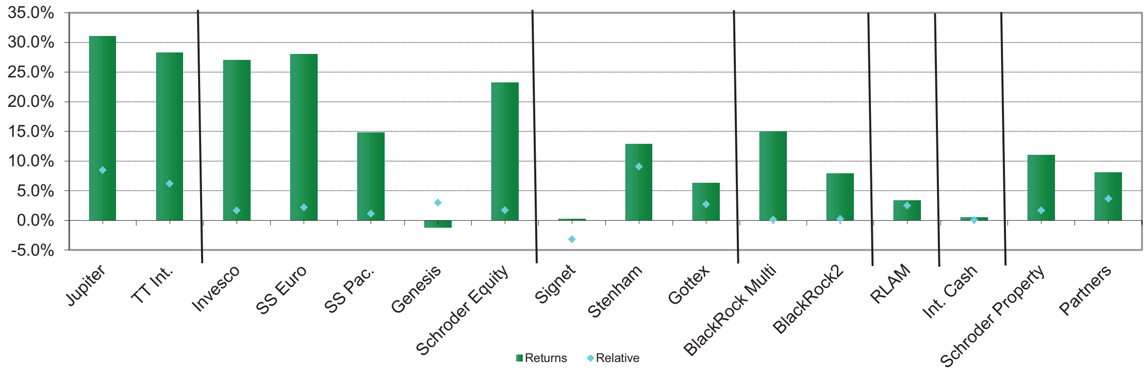
## Aggregate manager performance

The charts below show the absolute return for each manager over the quarter, one year and three years to the end of December 2013. The relative quarter, one year and three year returns are marked with green and blue dots respectively.

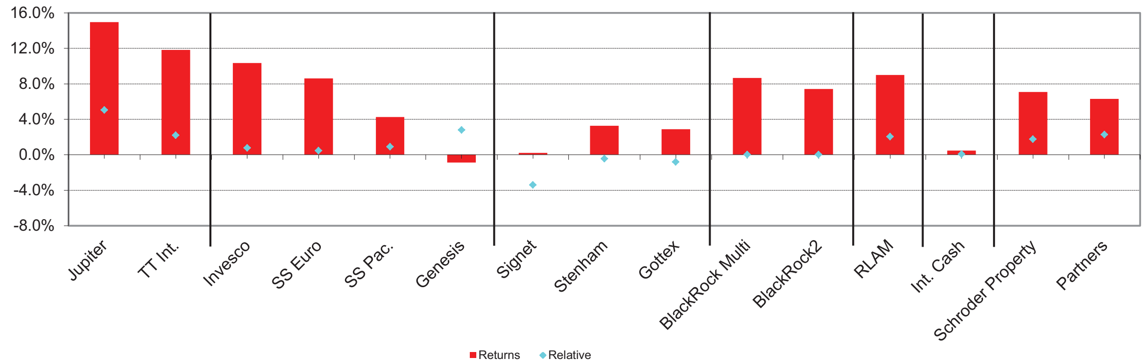
Absolute and relative performance - **Quarter to 31 December 2013**




Absolute and relative performance - **Year to 31 December 2013**




Absolute and relative performance - **3 years to 31 December 2013**




Source: Data provided by WM Performance Services

The table below shows the relative returns of each of the funds over the quarter, one year and three years to the end of December 2013. Returns in blue text are returns which outperformed the respective benchmarks, red text shows an underperformance, and black text represents performance in line with the benchmark.

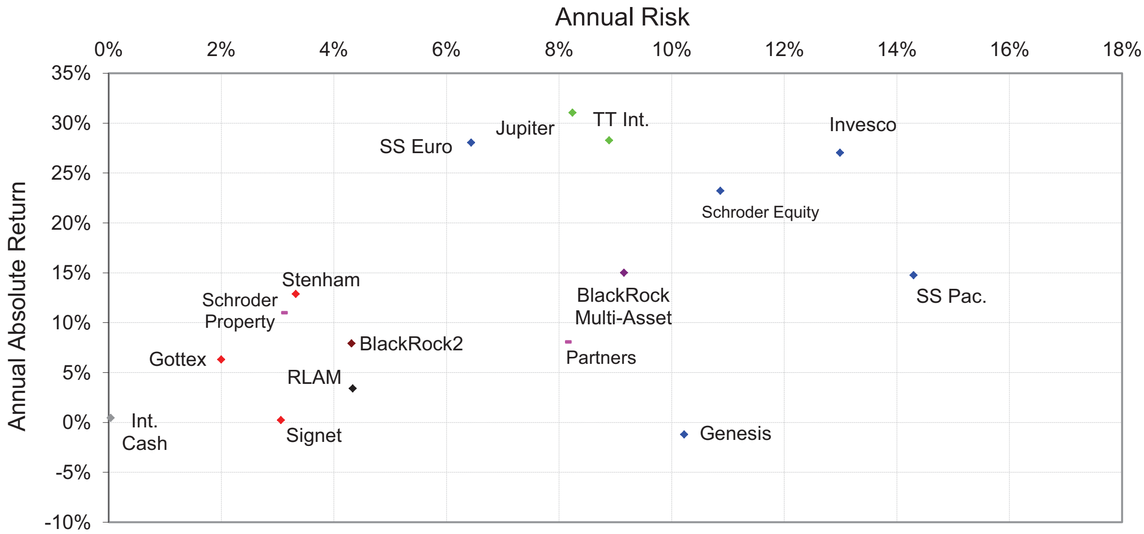
| Manager / fund | 3 months (%) | 1 year (%) | 3 years (% p.a.) | 3 year performance versus target |
|---|---|---|---|---|
| Jupiter | +2.1 | +8.5 | +5.1 | Target met |
| TT International | +3.2 | +6.2 | +2.2 | Target not met |
| Invesco | +0.2 | +1.7 | +0.8 | Target met |
| SSgA Europe | +0.8 | +2.2 | +0.5 | Target met |
| SSgA Pacific | +0.2 | +1.1 | +0.9 | Target met |
| Genesis | +0.1 | +3.0 | +2.8 | Target met |
| Schroder Equity | +0.9 | +1.7 | NA | N/A |
| Signet | 0.0 | -3.2 | -3.4 | Target not met |
| Stenham | +3.8 | +9.1 | -0.4 | Target not met |
| Gottex | +1.3 | +2.7 | -0.8 | Target not met |
| BlackRock Multi - Asset | +0.2 | +0.1 | 0.0 | Target met |
| BlackRock 2 | -0.1 | +0.3 | 0.0 | Target met |
| RLAM | +0.7 | +2.5 | +2.1 | Target met |
| Internal Cash | 0.0 | +0.1 | +0.1 | N/A |
| Schroder Property | +0.6 | +1.7 | +1.8 | Target met |
| Partners Property | -6.0 | +3.7 | +2.3 | N/A |

Source: Data provided by WM Performance Services

## Manager and Total Fund risk v return

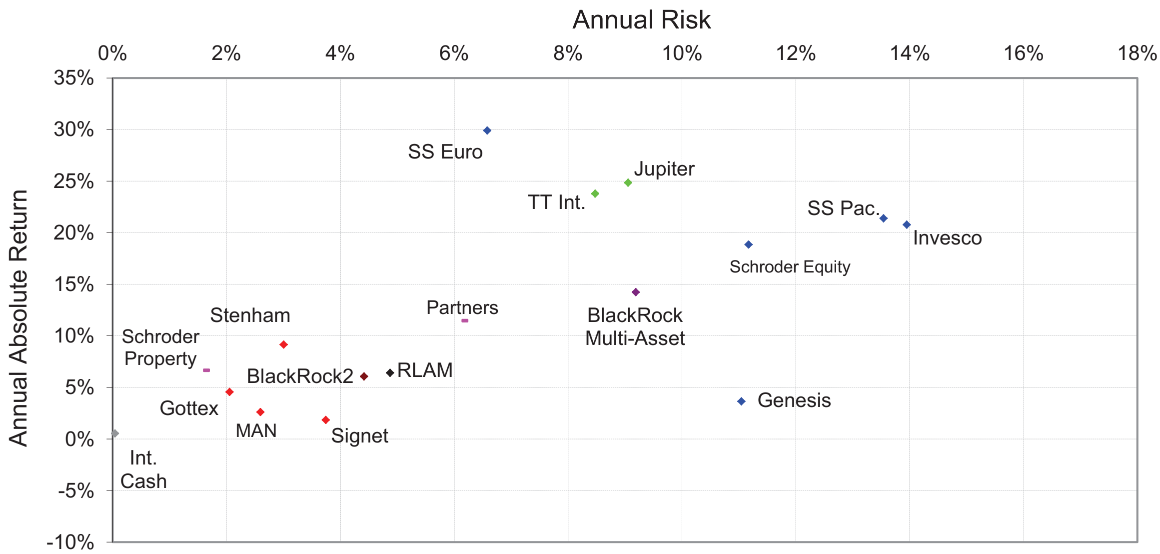
The chart below shows the 1 year absolute return ("Annual Absolute Return") against the 1 year volatility of absolute returns ("Annual Risk"), based on monthly/quarterly (as available) data points in sterling terms, to the end of December 2013 of each of the funds. We also show the same chart, but with data to 30 September 2013 for comparison.

**1 Year Risk v 1 Year Return to 31 December 2013**




Source: Data provided by WM Performance Services

**1 Year Risk v 1 Year Return to 30 September 2013**




Source: Data provided by WM Performance Services

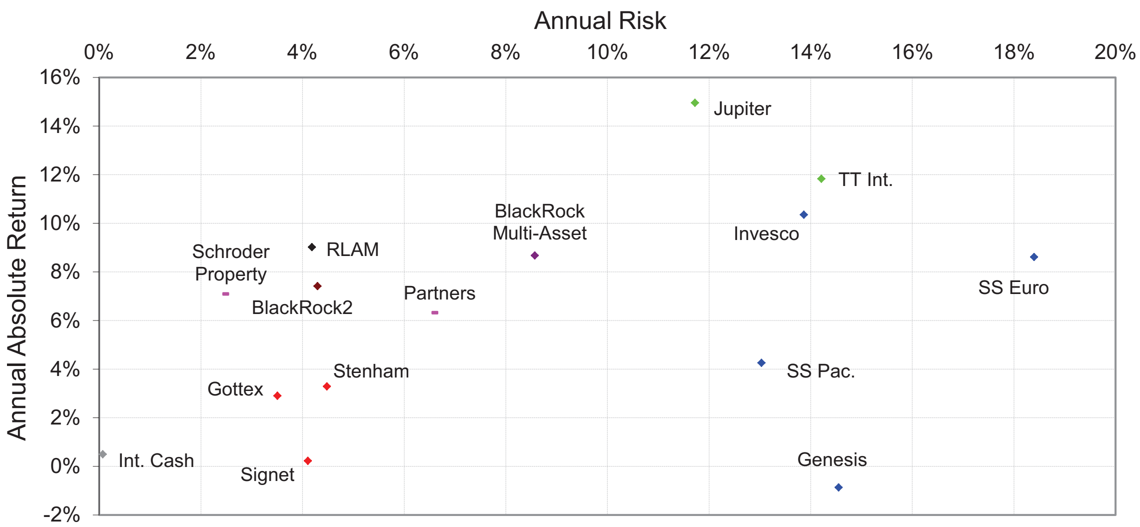
The managers are colour coded by asset class, as follows:

- Green: UK equities — Blue: overseas equities
- Red: fund of hedge funds — Black: bonds
- Maroon: multi-asset — Brown: BlackRock No. 2 portfolio
- Grey: internally managed cash — Pink: Property
- Green Square: total Fund

- The highest one-year returns came from the UK equity managers, with Jupiter at 31.0% and TT at 28.3%. Marginally behind were Invesco, SSgA Europe and Schroder equity, all with returns above 20%.
- SSgA Pacific and Genesis were affected by relatively poor returns in Asia and the emerging markets. The Genesis emerging equity return has fallen from 3.6% to -1.2%.
- Other notable movements in the one-year return were Schroders Property (up from 6.7% to 11.0%) and RLAM (down from 6.4% to 3.4%)
- The one year-risk figures have remained reasonably stable, apart from Schroders Property (up from 1.6% to 3.1%) whose last quarter's return was significantly higher than the more stable lower returns of the previous four quarters.

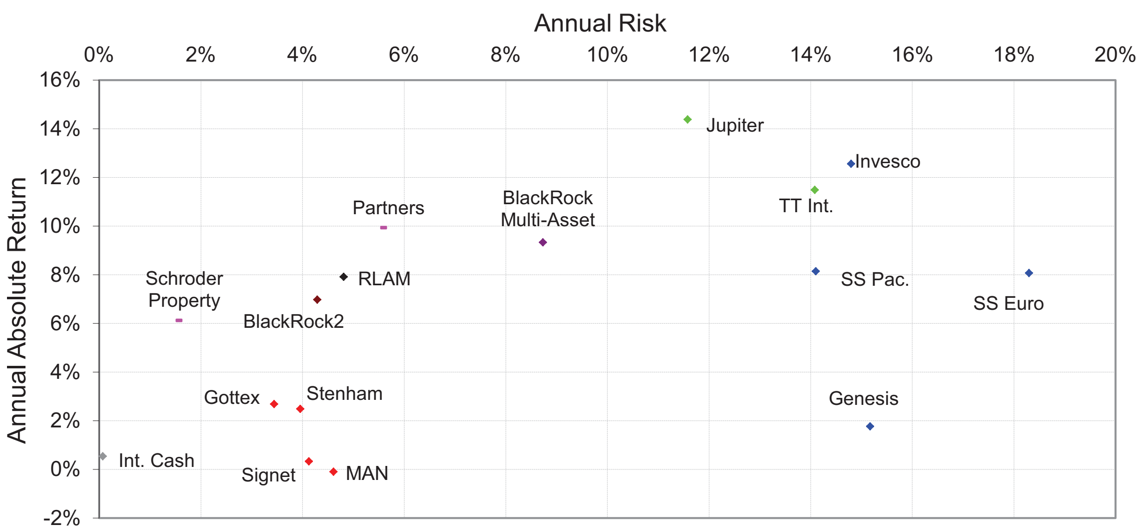
The chart below shows the 3 year absolute return ("Annual Absolute Return") against the 3 year volatility of absolute returns ("Annual Risk"), based on monthly/quarterly (as available) data points in sterling terms, to the end of December 2013 of each of the funds. We also show the same chart, but with data to 30 September 2013 for comparison.

**3 Year Risk v 3 Year Return to 31 December 2013**




Source: Data provided by WM Performance Services

**3 Year Risk v 3 Year Return to 30 September 2013**




Source: Data provided by WM Performance Services

The managers are colour coded by asset class, as follows:

- Green: UK equities — Blue: overseas equities
- Red: fund of hedge funds — Black: bonds
- Maroon: multi-asset — Brown: BlackRock No. 2 portfolio
- Grey: internally managed cash — Pink: Property
- Green Square: total Fund

- The three-year returns have remained reasonably stable apart from the emerging market and Asia equity managers.
- SSgA Pacific's return has fallen from 8.1% p.a. to 4.3% p.a. and Genesis from 1.8% p.a. to -0.9% p.a. Both managers continue to outperform their respective benchmarks.
- The three-year risk figures have also remained stable. As would be expected, the equity-based funds have the highest volatility and hedge funds, property and fixed interest the lowest, in line with the market returns chart on page 8.

## Conclusion

- The strongest returns over the one year period are from the equity funds. The one-year return was positive in absolute terms from all managers except for Genesis.
- Over three years, the best performer remains Jupiter at 15.0% p.a., some margin above the second best, TT, at 11.8% p.a.
- Hedge fund returns remain the lowest at around -2% p.a to 3% p.a. together with Genesis at -0.9% p.a.
- Generally returns were broadly consistent with those seen last quarter, with the exception of Genesis emerging markets equity and SSgA Pacific equity.
- The Fund of Hedge Fund and property managers continue to provide low volatility over both the 1 and three year period. However, over the longer three year period Fund of Hedge Funds have underperformed their assumed strategic return.

# 5 Individual Manager Performance

This section provides a one page summary of the key risk and return characteristics for each investment manager. An explanatory summary of each of the charts is included in the Glossary in Appendix A, with a reference for each chart in the chart title (e.g. #1). A summary of mandates is included in Appendix B, which shows the benchmark and outperformance target for each fund.

## Key points for consideration

- In a period of underperformance from Asia (ex Japan) and Emerging Markets relative to other equity regions, SSgA (Asia Pacific) and Genesis (Emerging Markets) have been able to outperform their respective benchmarks.
- The Fund's returns over the past three years have benefited from a high allocation to equities and from its bond holdings, with both returning significantly above the assumed strategic return over this period.
    - Returns from both asset classes are unlikely to be as high over the following three years given current low bond yields and deleveraging consumers and governments.
    - The Fund's exposure to alternative asset classes and changes being made as a result of the recent strategic review should provide diversification to equities and bonds.
- Whilst it is too short a period to draw any concrete conclusions, there does not appear to have been any immediate negative impact on the performance of the Schroder Global Equity Portfolio following the departure of Virginie Maisonneuve.

## 5.1 Jupiter Asset Management - UK Equities (Socially Responsible Investing)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| UK equities (Socially Responsible Investing) | FTSE All Share | +2% | April 2001 |

**Reason in Portfolio**

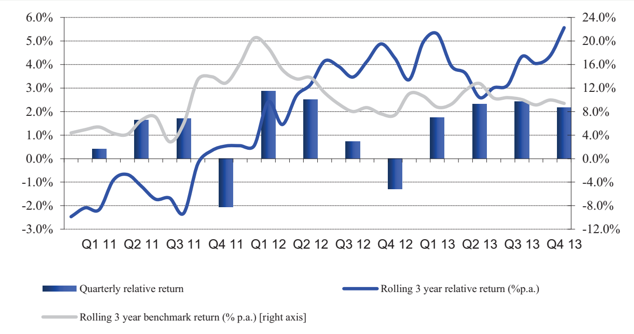
To provide asset growth as part of diversified equity portfolio

**Reason Manager Selected**

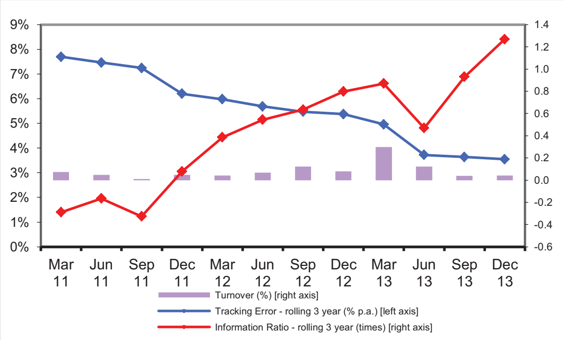
- Clear and robust approach to evaluating SRI factors within the investment process
- Dedicated team of SRI analysts to research SRI issues and lead engagement and voting activities
- Corporate commitment to SRI investment approach within a more mainstream investment team

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £163,577 | 5.0 | 5.0% | 58 |

**Relative returns** #1




**Tracking error, Information ratio, Turnover** #4




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 7.6 | 31.0 | 15.0 |
| Benchmark | 5.5 | 20.8 | 9.4 |
| Relative | +2.1 | +8.5 | +5.1 |

Source: Data provided by WM Performance Services, and Jupiter.

## Comments:

- Jupiter are significantly outperforming their 3 year performance target. Due to the nature of the portfolio (as outlined below), we would expect the fund return to exhibit differences relative to the FTSE All Share Index return and have no concern over the risk taken by the fund.
- The Fund's allocation to Cash (6.5%) has increased from the last quarter but remains below the 7% limit.
- The industry allocation has continued to remain considerably different to the benchmark allocation (as expected from Socially Responsible Investing), so the variability of relative returns (tracking error) is expected to be high. Over Q4 2013, Jupiter was significantly underweight in Oil & Gas, Consumer Goods and Basic Materials, with significant overweight positions in Consumer Services and Industrials.
- There was an increase in the information ratio over the quarter as the three-year return increased from 3.9% p.a. to 5.1% p.a.

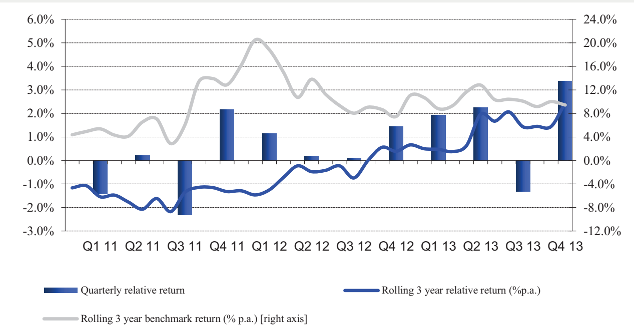
## 5.2 TT International – UK Equities (Unconstrained)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| UK equities (unconstrained) | FTSE All Share | +3-4% | July 2007 |

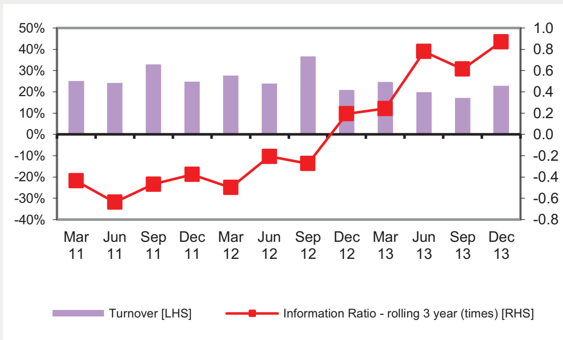
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ■ Favoured the partnership structure that aligns managers and Fund's interests.<br>■ Focussed investment activity and manages its capacity<br>■ Clear, robust stock selection and portfolio construction process |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £185,688 | 5.6 | 2.8% | 53 |

**Relative returns** [#1]




**Information ratio and Turnover** [#4]




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 8.8 | 28.3 | 11.8 |
| Benchmark | 5.5 | 20.8 | 9.4 |
| Relative | +3.2 | +6.2 | +2.2 |

Source: Data provided by WM Performance Services, and TT International.

### Comments:

- The Fund has outperformed the benchmark over the quarter, one year and three year periods, and is approaching their 3 year performance target.
- The Fund held an overweight position in Industrials by 5.3% and was underweight in Oil & Gas and Utilities, by 4.7% and 2.2% respectively, at the end of the quarter.
- Turnover, over the fourth quarter, increased to 22.8% compared to the last quarter's number of 17.2%.
- The 3 year tracking error (proxy for risk relative to the benchmark) has increased in Q4 2013, to stand at 2.76%. This is a first quarter of increase after a consistent decrease since Q3 2010, when it was 3.12%.
- The 3 year information ratio increased by 0.26 to 0.67, demonstrating an increase in the relative return.

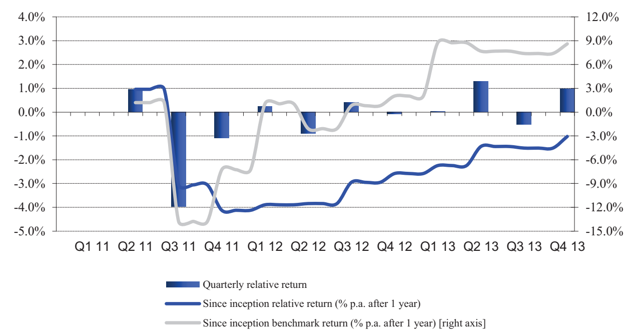
## 5.3 Schroder – Global Equity Portfolio (Unconstrained)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Global Equities (Unconstrained) | MSCI AC World Index Free | +4% | April 2011 |

| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ■ Clear philosophy and approach<br>■ Long term investment philosophy aligned with Fund's goals, commitment to incorporating ESG principles throughout the investment process<br>■ Evidence of ability to achieve the Fund's performance target |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £215,489 | 6.5 | N/A | N/A |

**Relative returns** [#1]




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 6.0 | 23.2 | N/A |
| Benchmark | 5.0 | 21.2 | N/A |
| Relative | +0.9 | +1.7 | N/A |

Source: Data provided by WM Performance Services, and Schroders.

### Comments:

- The return was above the benchmark over the quarter and 1 year period, but remains below their performance target over 1 year.
- Companies in "later-cycle sectors", such as capital goods, performed well, and Schroders expect this to continue in 2014. Financials stocks, such as insurance companies and US banks, also performed well.
- Negatives were emerging market equities, especially in Brazil where there was a slowdown in consumer spending. Concerns about the Indonesian economy affected their stock Jardine Strategic, which has operations in Indonesia. Schroders retain conviction in these stocks and view recent weakness as an opportunity to add to positions.
- Whereas equity returns in 2013 were largely driven by factors other than company earnings, in 2014 Schroders believe that earnings growth will be a more important driver of equity returns. The focus on company fundamentals will benefit stock-pickers, and the expected pick-up in global GDP growth will favour industrial stocks.
- Depressed bond yields have caused income-focused investors to search for income in the higher-yielding parts of the equity market. Schroders think this has pushed up the prices, making companies with strong future earnings and dividend growth look good value relative to income stocks.

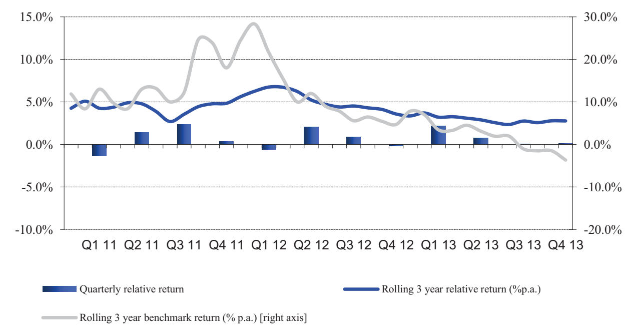
## 5.4 Genesis Asset Managers – Emerging Market Equities

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Emerging Market equities | MSCI EM IMI TR | - | December 2006 |

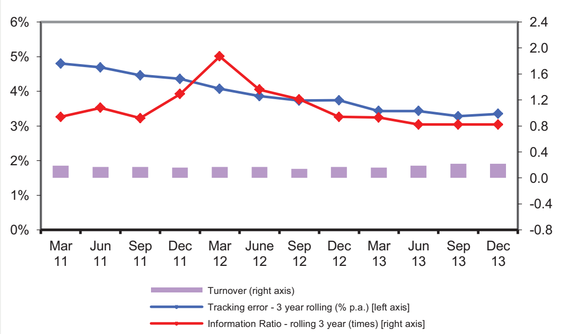
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ■ Long term investment approach which takes advantage of evolving growth opportunities<br>■ Niche and focussed expertise in emerging markets<br>■ Partnership structure aligned to delivering performance rather than growing assets under management |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £145,731 | 4.4 | 3.4% | 163 |

**Relative returns** [#1]




**Tracking error, Information ratio, Turnover** [#4]




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | -0.3 | -1.2 | -0.9 |
| Benchmark | -0.4 | -4.1 | -3.6 |
| relative | +0.1 | +3.0 | +2.8 |

Source: Data provided by WM Performance Services, and Genesis.

### Comments:

- Genesis have achieved significant outperformance of the benchmark over 3 years.
- The Fund is overweight to India, South Africa and Russia, while underweight to South Korea and China, although note that the over and underweights are a result of Genesis' stock picking approach, rather than taking a view on countries.
- The three year tracking error (proxy for risk relative to the benchmark) increased slightly to 3.4% in Q4 2013. The three year information ratio (risk adjusted return), has remained unchanged to 0.8.
- The allocation to Cash (1.4%) decreased slightly compared to the previous quarter (1.9%).
- On an industry basis, the Fund is overweight Consumer Staples (+7.6%), Materials (+5.7%), Health Care (+2.6%), Information Technology (+1.3%) and Financials (+0.8%). The Fund is underweight to Consumer Discretionary (-5.5%), Energy (-4.0%), Telecom Services (-4.6%), Industrials (-3.1%) and Utilities (-2.0%).

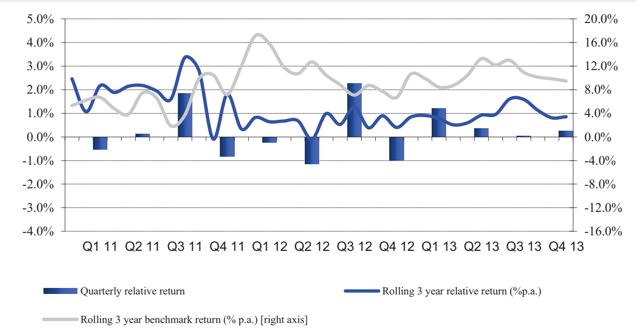
## 5.5 Invesco – Global ex-UK Equities (Enhanced Indexation)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Global ex-UK equities enhanced (En. Indexation) | MSCI World ex UK NDR | +0.5% | December 2006 |

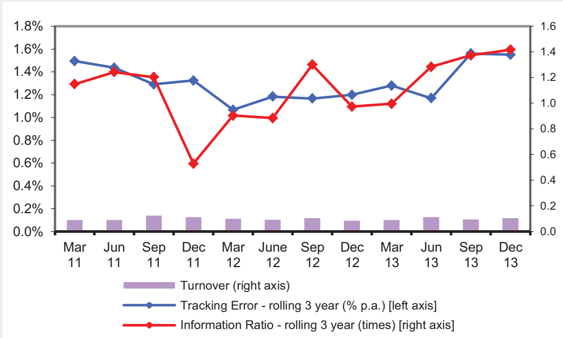
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ■ Robust investment process supported by historical performance record, providing a high level of assurance that the process could generate the outperformance target on a consistent basis<br>■ One of few to Offer a Global ex UK pooled fund |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £236,622 | 7.2 | 1.6% | 385 |

**Relative returns** #1




**Tracking error, Information ratio, Turnover** #4




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 5.9 | 27.0 | 10.4 |
| Benchmark | 5.7 | 25.0 | 9.5 |
| relative | +0.2 | +1.7 | +0.8 |

Source: Data provided by WM Performance Services, and Invesco.

### Comments:

- Over the last quarter, stock selection contributed positively.
- The absolute volatility has increased to 11.4% at the end of the fourth quarter of 2013 compared to 11.0% at the end of the third quarter of 2013, reflecting the increase in market volatility over the period.
- The turnover for this quarter of 10.5% increased from 9.3% in the previous quarter. The number of stocks (385) increased compared to the previous quarter. It remains an appropriate number for the enhanced indexation approach.
- The industry allocation is relatively in line with the benchmark industry allocations. All industry allocations were broadly within +/- 1.0% of benchmark weightings.
- Invesco's three year performance remains above their outperformance target.

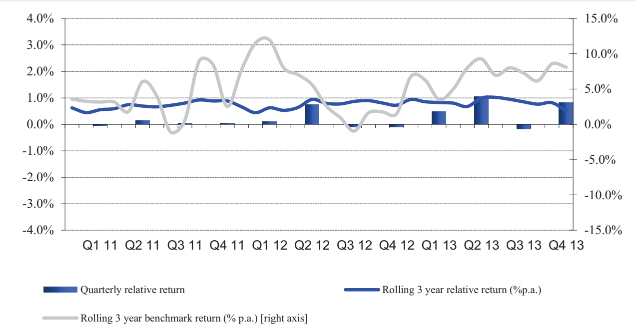
## 5.6 SSgA – Europe ex-UK Equities (Enhanced Indexation)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Europe ex-UK equities (enhanced indexation) | FTSE AW Europe ex UK | +0.5% | December 2006 |

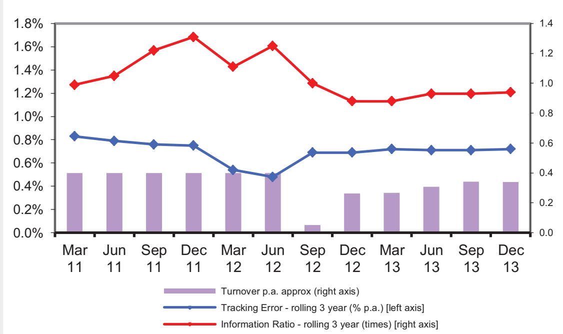
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ▪ Strength of their quantitative model and process, and ongoing research to develop the model.<br>▪ Historical performance met the risk return parameters the Fund was seeking.<br>▪ 2 Funds (European and Pacific) to achieve the Fund's customised asset allocation within overseas equities |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £39,903 | 1.2 | 0.7 | 212 |

**Relative returns [#1]**




**Tracking error, Information ratio, Turnover [#4]**




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 6.5 | 28.0 | 8.6 |
| Benchmark | 5.7 | 25.3 | 8.1 |
| relative | +0.8 | +2.2 | +0.5 |

Source: Data provided by WM Performance Services, and SSgA.

### Comments:

- The Fund's return is meeting their performance target over 3 years.
- France, Germany and Switzerland make up over 60% of the fund's benchmark - it remains overweight in all three countries.
- The total pooled fund size on 31 December 2013 was £39.98m, increasing over the last quarter and falling significantly since the size of £306.12m on 31 March 2011. Performance of the SSgA Europe ex UK Enhanced Equity Fund does not appear to have been affected by its reduction in size.
- Turnover has decreased from 34.2% to 33.9%, closer to that previously seen. The tracking error has remained more or less in line with the previous quarter.
- The information ratio has broadly remained the same as compared to the previous quarter.

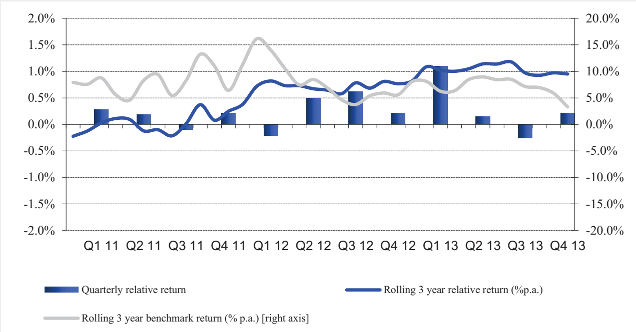
## 5.7 SSgA – Pacific incl. Japan Equities (Enhanced Indexation)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Pacific inc. Japan equities | FTSE AW Dev Asia Pacific | +0.5% | December 2006 |

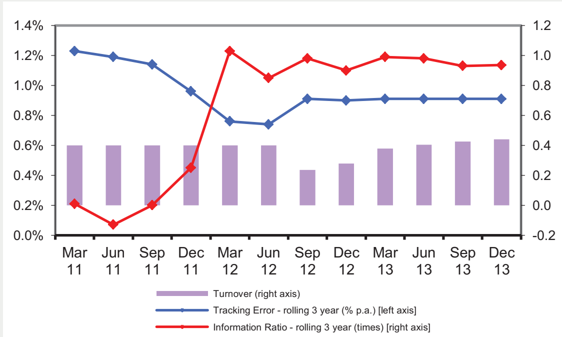
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified equity portfolio | ■ Strength of their quantitative model and process, and ongoing research to develop the model.<br>■ Historical performance met the risk return parameters the Fund was seeking.<br>■ 2 Funds (European and Pacific) to achieve the Fund's customised asset allocation within overseas equities |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Holdings |
|---|---|---|---|
| £67,896 | 2.1 | 0.9 | N/A |

**Relative returns [#1]**




**Tracking error, Information ratio, Turnover [#4]**




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | -0.3 | 14.8 | 4.3 |
| Benchmark | -0.5 | 13.5 | 3.3 |
| Relative | +0.2 | +1.1 | +0.9 |

Source: Data provided by WM Performance Services, and SSgA.

### Comments:

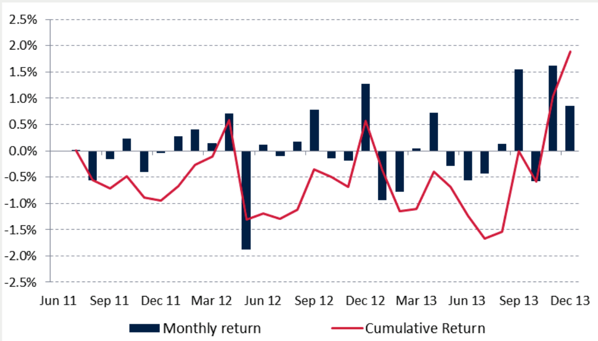
- In terms of country allocation, there are no significant deviations away from the benchmark. Just over half of the fund (56.3%) is invested in Japan, increasing from 55.8% last quarter in line with the benchmark.
- The pooled fund size is £69.96m of which Avon hold £67.90m. As with the European fund, the conclusion has been that the Fund could be sustained even if the Avon Pension Fund was the only investor.
- The fund outperformed over the quarter and it remains ahead of their performance target over the one and three year periods as well.
- Turnover has further increased to 44.1% after an increase in the previous quarter as well.
- The information ratio (+0.94) has slightly increased compared to the previous quarter (+0.93).
- The tracking error of the fund has remained the same as it was last quarter.

## 5.8 Record – Active Currency Hedging

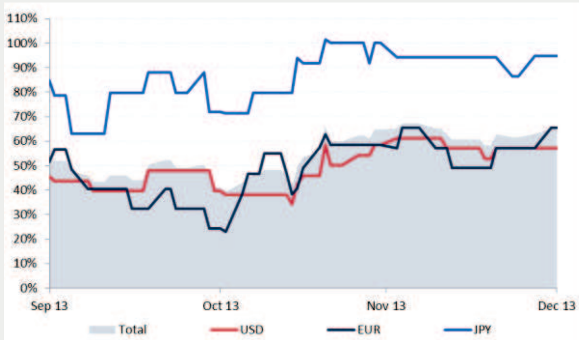
| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Dynamic Currency Hedge (US$, Yen and Euro equity exposure) | N/A | N/a | July 2011 |

| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To manage the volatility arising from overseas currency exposure, whilst attempting to minimise negative cashflows that can arise from currency hedging. | ■ Straightforward technical (ie based on price information) process<br>■ Does not rely on human intervention<br>■ Strong IT infrastructure and currency specialists |

**Hedging Return**




**Hedging Ratios**




**Performance (Total Hedging Portfolio)**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Record Hedge | 1.89 | 1.30 | n/a |
| 50% Illustrative Hedge | 1.43 | 1.83 | n/a |
| Relative | 0.46 | -0.53 | n/a |

**Currency Hedging 3 Month Performance in Sterling Terms**

| | Start Exposure (£) | End Exposure (%) | Currency Return (%) | 50% Hedge Return (%) | Record Hedge Return (%) |
|---|---|---|---|---|---|
| USD | 577,173,871 | 479,204,874 | -2.22 | 1.14 | 1.22 |
| EUR | 218,624,097 | 200,118,065 | -0.47 | 0.26 | -0.31 |
| JPY | 143,159,655 | 125,312,152 | -8.72 | 4.53 | 8.30 |
| **Totals** | **938,957,622** | **804,635,091** | **-2.79** | **1.43** | **1.89** |

Source: Record Currency Management. Note: Exposures are 1 month lagged. Returns are estimated by JLT.

### Comments:

- Sterling strengthening has meant that the impact of currency hedging has had a beneficial impact.
- Over the most recent quarter, Record have outperformed a 50% hedge against the USD and Yen, but underperformed a 50% hedge against the Euro.
- The overall hedging ratio remains towards the peak of the period since inception.

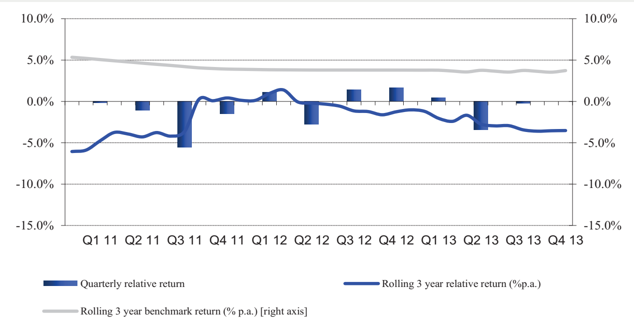
## 5.9 Signet – Fund of Hedge Funds

| Mandate | Benchmark | Portfolio Volatility (3 yr p.a.) | Inception Date |
|---|---|---|---|
| Fund of Hedge Funds | 3 month LIBOR +3.0% | 4.8% | August 2007 |

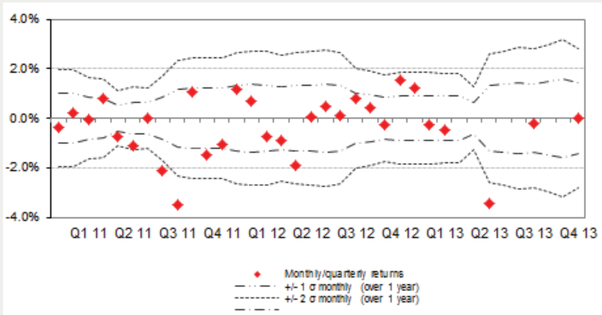
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To reduce the volatility of the Growth portfolio and increase diversification | ■ Niche fixed income strategy focus<br>■ Established team with strong track record<br>■ Complemented other funds in portfolio |

| Value (£'000) | % Fund Assets | Number of Funds |
|---|---|---|
| £66,477 | 2.0 | 27 |

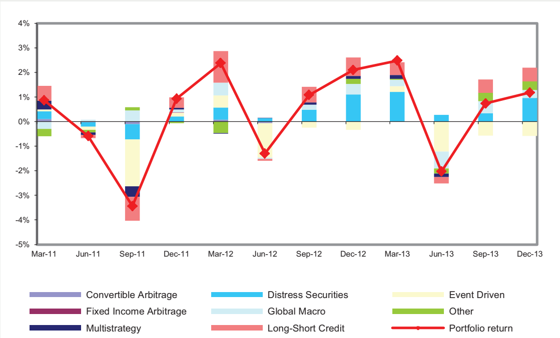
### Relative returns [#1]



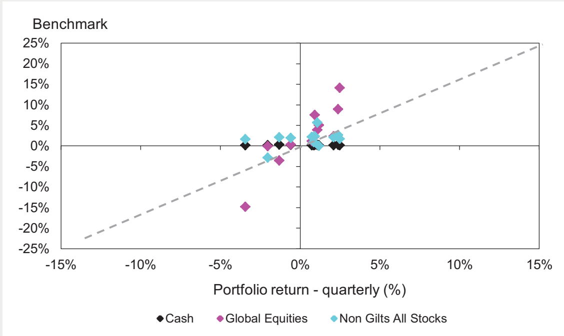

### Monthly relative returns [#2]




### Hedge fund strategies and source of return [#6]




### Correlation with indices [#7]




### Performance

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 0.9 | 0.2 | 0.2 |
| Benchmark | 0.9 | 3.5 | 3.7 |
| relative | 0.0 | -3.2 | -3.4 |

Source: Data provided by WM Performance Services, and Signet.

## Comments:

- Signet are underperforming their target over both 1 year and 3 years, despite a quarterly return this quarter in line with their target.
- The main contributor to Signet's quarterly performance was Distressed (1.0%), offset by Event-Driven and Special Situations (-0.6%). Both of these strategies were around 16% of the fund's asset allocation.
- There is little correlation between this Fund and cash or non gilt bonds, but a weak correlation with global equities. This suggests that this Fund acts as a good diversifier to other asset classes.

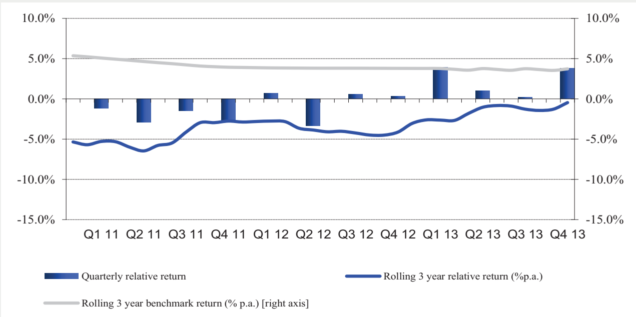
## 5.10 Stenham – Fund of Hedge Funds

| Mandate | Benchmark | Portfolio Volatility (3 yr p.a.) | Inception Date |
|---|---|---|---|
| Fund of Hedge Funds | 3 month LIBOR +3.0% | 3.5% | August 2007 |

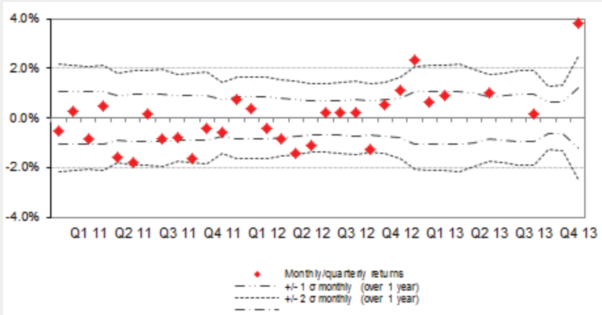
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To reduce the volatility of the Growth portfolio and increase diversification | ■ Focussed multi-strategy approach, concentrating on long / short equity, global macro and event driven strategies<br>■ Established team, strong track record at selecting managers<br>■ Complemented other funds in portfolio |

| Value (£'000) | % Fund Assets | Number of Funds Over The Period |
|---|---|---|
| £37,657 | 1.1 | 17 |

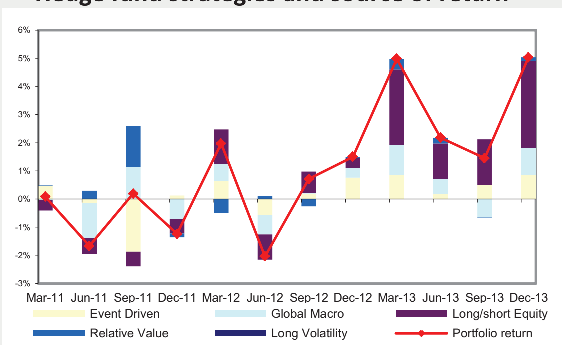
**Relative returns** #1



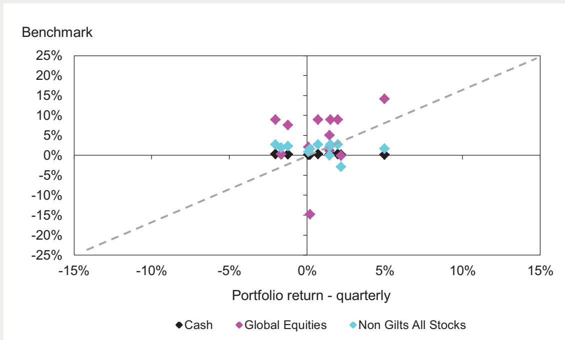

**Monthly relative returns** #2




**Hedge fund strategies and source of return** #6




**Correlation with indices** #7




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 4.7 | 12.9 | 3.3 |
| Benchmark | 0.9 | 3.5 | 3.7 |
| Relative | +3.8 | +9.1 | -0.4 |

Source: Data provided by WM Performance Services, and Stenham.

**Comments:**

- In 2013 Stenham changed the focus of its business strategy, focussing away from growing its institutional business to focus on existing investors and strategic acquisition and joint venture projects.
- There has been stronger performance since Stenham adopted a more positive outlook and returned to confidence in fundamentals as a driver of returns. Stenham have outperformed their target over three months and one year but are still behind over the three year measure.
- The main positive contribution to performance came from Long/short Equity (3.1%). Global Macro (1.0%), Event Driven (0.9%) and Relative Value (0.1%) also contributed positively.
- The allocation to the Global Macro and Long / Short Equity strategies made up 72.0% of the total Fund allocation. The allocation to Cash remained the same over the quarter.
- The number of funds have remained the same at 17.
- There is no clear correlation between this Fund and cash, global equities or non gilt bonds. This suggests that this Fund acts as a good diversifier to the Avon Pension Fund's other asset classes.

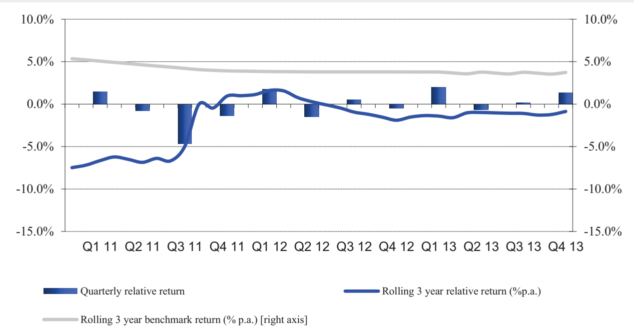
## 5.11 Gottex – Fund of Hedge Funds

| Mandate | Benchmark | Portfolio Volatility (3 yr p.a.) | Inception Date |
|---|---|---|---|
| Fund of Hedge Funds | 3 month LIBOR +3.0% | 2.7% | August 2007 |

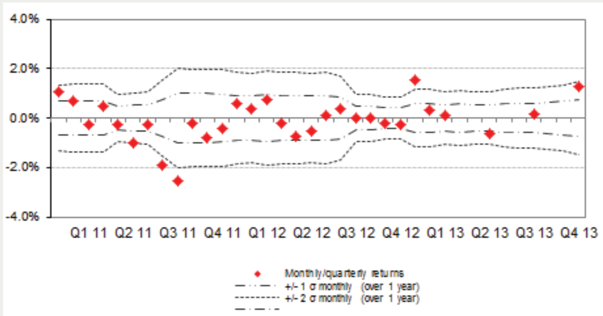
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To reduce the volatility of the Growth portfolio and increase diversification | ■ Niche market neutral investment strategy<br>■ Established team, strong track record<br>■ Complemented other funds in portfolio |

| Value (£'000) | % Fund Assets | Number of Funds |
|---|---|---|
| £56,953 | 1.7 | Not available |

**Relative returns** [#1]

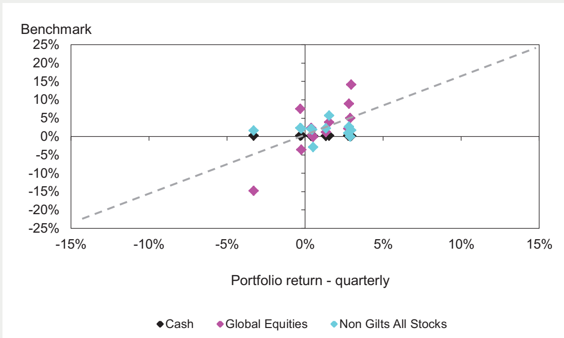



**Monthly relative returns** [#2]




**Hedge fund strategies and source of return** [#6]


**Correlation with indices** [#7]




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 2.1 | 6.3 | 2.9 |
| Benchmark | 0.9 | 3.5 | 3.7 |
| Relative | +1.3 | +2.7 | -0.8 |

Source: Data provided by WM Performance Services, and Gottex.

### Comments:

- In December Gottex announced a merger with EIM. The Panel are meeting Gottex and can assess the potential impact of the proposed merger.
- The Fund has a diverse range of strategy exposures, with continued major exposures to Asset Backed Securities, Mortgage Backed Securities and Fundamental MN Equity strategies. The allocation to Long-short equity and Event-driven equity were increased over the quarter.
- Gottex have outperformed their target over 12 months but remain behind over 3 years.
- There is no clear correlation between this Fund and cash or non-gilt bonds, and a weak correlation with global equities. This suggests that this Fund acts as a good diversifier to the Avon Pension Fund's other asset classes.

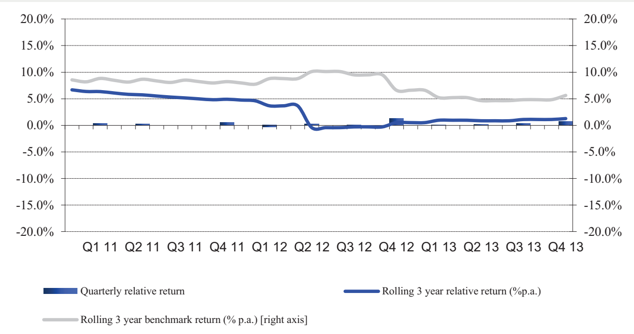
## 5.12 Schroder – UK Property

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| UK property | IPD UK pooled | +1.0% | February 2009 |

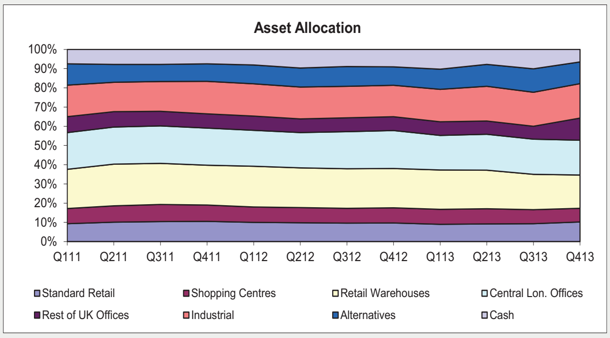
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To reduce the volatility of the Growth portfolio and increase diversification | ■ Demonstrable track record of delivering consistent, above average performance.<br>■ Team though small is exclusively dedicated to UK multi-manager property management but can draw on the extensive resources of the Schroders direct property team.<br>■ Well structured and research orientated investment process. |

| Value (£'000) | % Fund Assets | Tracking Error | Number of Funds |
|---|---|---|---|
| £146,148 | 4.4 | Not available | 16 |

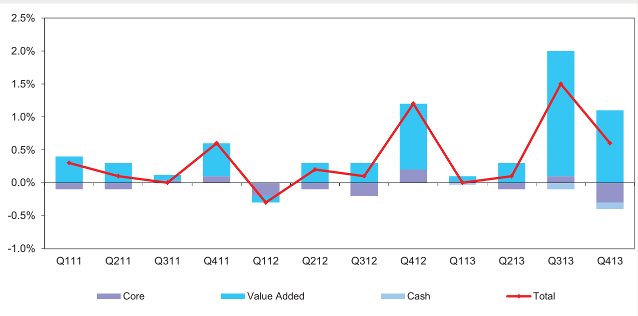
**Relative returns** [#1]




**Asset Allocation** [#5]




**Contribution to relative return** [#6]




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 4.9 | 11.0 | 7.1 |
| Benchmark | 4.3 | 9.2 | 5.2 |
| relative | +0.6 | +1.7 | +1.8 |

Source: Data provided by WM Performance Services, and Schroders.

**Comments:**

- Schroder were appointed to manage UK Property on a segregated, multi-manager basis. The investments held within the underlying funds are primarily direct, although some managers might use listed securities for diversification.
- Over the quarter, the fund outperformed the benchmark. The three year performance also remains strong, exceeding the benchmark by 1.6% per annum.
- Once again, central London exposure, particularly to the West End and offices, made a significant contribution to the return.
- Value added funds, some of which employ moderate leverage, produced the strongest results. Core funds detracted from returns due to the transaction costs of switching between two underlying property funds (Schroder sold M&G UK Property Fund to invest in Metro PUT as they believe the Metro fund offers better performance prospects as it has increased the portfolio's exposure to South East offices where more generous investment yields are on offer).
- Whereas London has led the revival to date, Schroder also expect to see improvements in occupational markets away from the capital in 2014. They have increased the portfolios exposure to South East offices, as a shortage of Grade A offices is putting upward pressure on rents.
- Schroder expect the recovery in UK commercial property to continue through 2014, with double digit returns, partly driven by the belief that there will not be an early rise in interest rates.

## 5.13 Partners – Overseas Property

| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To reduce the volatility of the Growth portfolio and increase diversification | ■ Depth of experience in global property investment and the resources they committed globally to the asset class.<br>■ The preferred structure for the portfolio was via a bespoke fund of funds (or private account) so the investment could be more tailored to the Fund's requirements. |

- The mandate awarded to Partners by the Fund commenced in August 2009, although draw downs are being made gradually over time, and the full extent of the Fund's commitment has not yet been invested.
- Partners invest in direct, primary and secondary private real estate investments on a global basis.

### Portfolio update

To date, Partners have drawn down approximately £113 million. A total of £9.75 million was drawn down over the quarter, around half of which was to Global Real Estate 2013, the first major draw down on this fund. The draw downs commenced in September 2009.

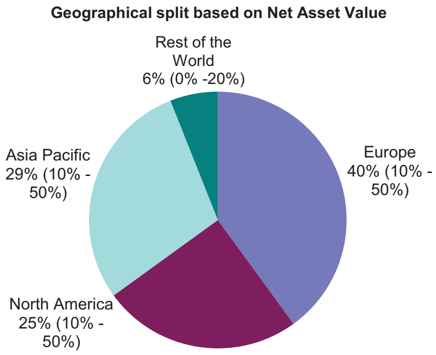
The funds invested to date have been split by Partners as follows:

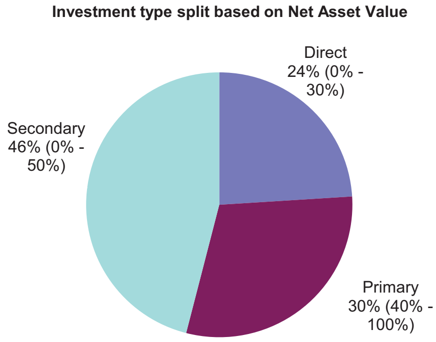
| Partners Fund | Net Drawn Down (£ Million) | Net Asset Value as at 31 December 2013 (£ Million) | Since Inception Net IRR |
|---|---|---|---|
| Real Estate Secondary 2009 | 16.52 | 17.65 | 11.9 |
| Global Real Estate 2008 | 30.36 | 26.31 | 7.9 |
| Asia Pacific and Emerging Market Real Estate 2009 | 13.84 | 13.08 | 6.9 |
| Distressed US Real Estate 2009 | 14.76 | 12.42 | 9.8 |
| Global Real Estate 2011 | 19.08 | 18.52 | 6.5 |
| Direct Real Estate 2011 | 10.35 | 10.48 | 6.5 |
| Real Estate Secondary 2013 | 3.25 | 3.87 | 19.2 |
| Global Real Estate 2013 | 5.17 | 5.31 | 11.3 |
| **Total** | **113.33** | **107.63** | **8.7** |

Source: Partners. (adjusted for cash flows), the above is Partners' valuation as at 31 December 2013.

The Net IRR is as expected, and in line with the mandate expectation.

The investments in the funds noted above have resulted in a portfolio that was, as at 31 December 2013, split regionally as shown in the chart on the left below, and across different investment types as shown on the right. We show in brackets for each region the current guideline allocations to each region that are in place for the Fund's portfolio.




Source: Partners

The allocation to Europe has increased over the quarter (from 33% to 40%), with decreases in North America (from 28% to 25%) and Asia Pacific (form 32% to 29%). These remain within the guidelines.

The exposure to Secondary has increased by 4% this quarter, with both Primary and Direct decreasing by 2%. Primary exposure continues to be below the guidelines. Short-term deviation from the guidelines are expected whilst the amount drawn-down is still significantly below target, and we do not believe the current positioning to be of concern. In total, 50% of the commitments are allocated to primary investments.

## Performance

Distributions since inception total £24.28m, with distributions worth £3.47m over the most recent quarter. Performance of Partners is lagged by 1 quarter. Over Q3 2013, the manager produced a return of -3.8% compared to the benchmark of 2.4%.

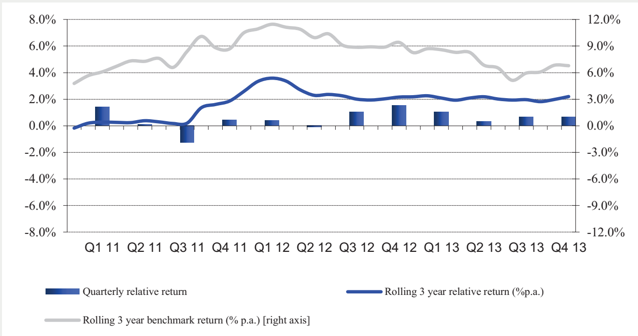
## 5.14 Royal London Asset Management – Fixed Interest

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| UK Corporate Bonds | iBoxx £ non-Gilts all maturities | +0.8% | July 2007 |

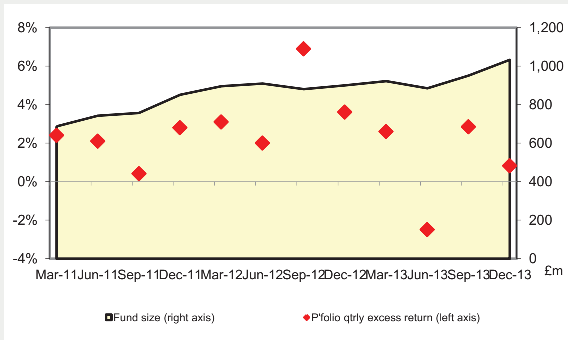
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To maintain stability in the Fund as part of a diversified fixed income portfolio | ■ Focused research strategy to generate added value<br>■ Focus research on unrated bonds provided a "niche" where price inefficiencies more prevalent<br>■ Product size means can be flexible within market |

| Value (£'000) | % Fund Assets | Number of Holdings |
|---|---|---|
| £242,148 | 7.3 | 250 |

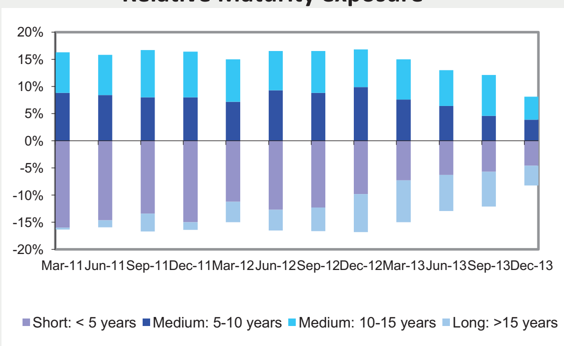
**Relative returns** #1



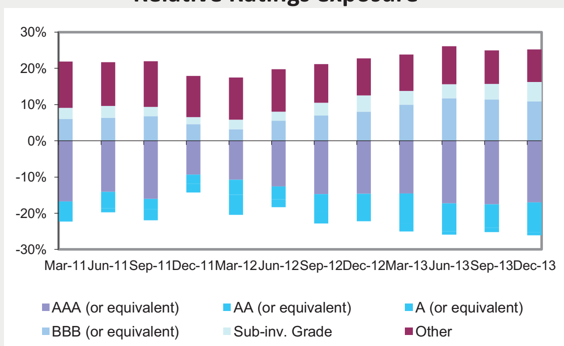

**Performance v fund size** #3



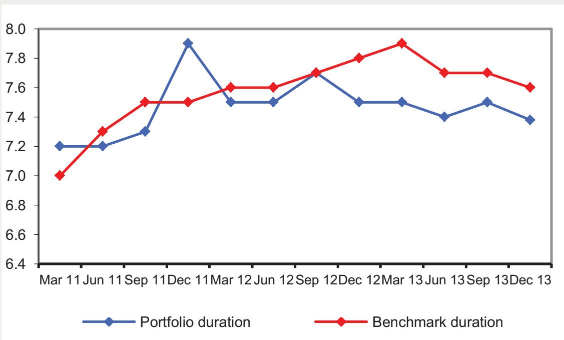

**Relative Maturity exposure** #8




**Relative Ratings exposure** #9




**Duration** #10




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 0.7 | 3.4 | 9.0 |
| Benchmark | 0.0 | 0.9 | 6.8 |
| relative | +0.7 | +2.5 | +2.1 |

Source: Data provided by WM Performance Services, and RLAM

## Comments:

- RLAM have maintained a consistent philosophy for some time - the Fund remains significantly underweight to AAA and to a lesser extent AA and A rated bonds, and overweight BBB and unrated bonds. This has benefited performance and resulted in significant outperformance at the high end of expectations for a mandate of this type.
- Similarly, RLAM favour medium term maturity bonds. This quarter they have moved to a less underweight position in long (over 15 year) bonds.
- Performance relative to the benchmark may be volatile in the short term due to RLAM's allocation to unrated bonds. These investments are not necessarily riskier or "junk status" and RLAM place their own rating on the bonds using their own research.

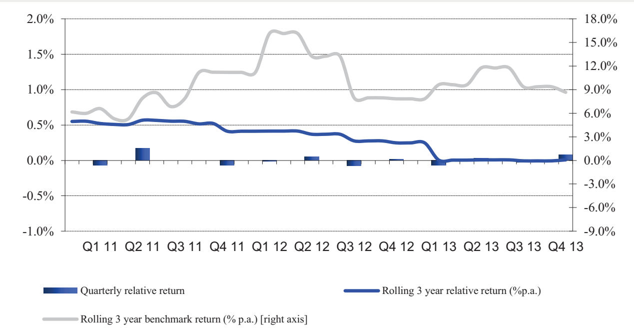
## 5.15 BlackRock – Passive Multi-Asset

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Passive multi-asset | In line with customised benchmarks using monthly mean fund weights | 0% | April 2003 |

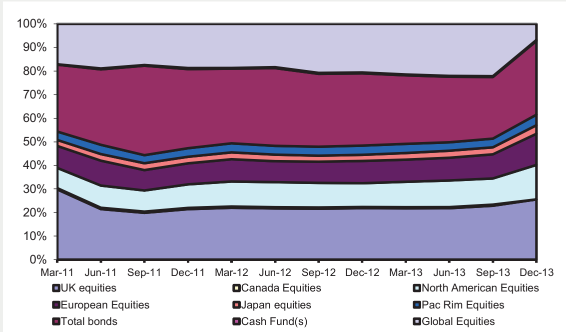
| Reason in Portfolio | Reason Manager Selected |
|---|---|
| To provide asset growth as part of diversified portfolio | ■ To provide low cost market exposure across multi asset classes<br>■ Provide efficient way for rebalancing between bonds and equities within a single portfolio |

| Value (£'000) | % Fund Assets |
|---|---|
| £1,170,637 | 35.5 |

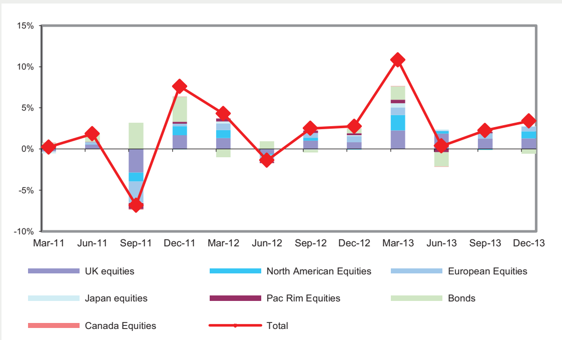
**Relative returns** #1




**Asset Allocation** #5




**Contribution to absolute return** #6




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 3.5 | 15.0 | 8.7 |
| Benchmark | 3.3 | 14.8 | 8.6 |
| relative | +0.2 | +0.1 | 0.0 |

Source: Data provided by WM Performance Services, and BlackRock

### Comments:

- Being a passive mandate, with a customised benchmark based on the monthly mean fund weights, there is nothing unusual arising in risk and performance.
- The magnitude of the relative volatility in the portfolio remains small.
- This quarter the global equity fund was sold down to fund the investments in DGFs.

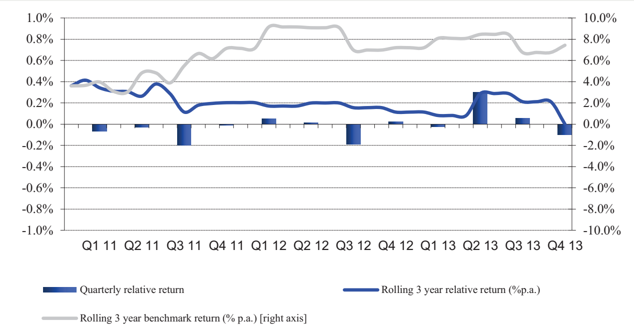
## 5.16 BlackRock No.2 – Property account (“ring fenced” assets)

| Mandate | Benchmark | Outperformance Target | Inception Date |
|---|---|---|---|
| Overseas property | Customised benchmarks using monthly mean fund weights | 0% | September 2009 |

| Reason in Portfolio | Reason Manager Selected |
|---|---|
| This portfolio was created to hold the assets intended for investment into Property. | BlackRock were the Fund’s passive provider and ‘swing fund’ and offered the most efficient solution at the time the portfolio was created. |

| Value (£'000) | % Fund Assets |
|---|---|
| £45,915 | 1.4 |

**Relative returns [#1]**




**Performance**

| | 3 months (%) | 1 year (%) | 3 years (% p.a.) |
|---|---|---|---|
| Fund | 2.4 | 7.9 | 7.4 |
| Benchmark | 2.4 | 7.6 | 7.4 |
| relative | -0.1 | +0.3 | 0.0 |

Source: Data provided by WM Performance Services, and BlackRock

### Comments:

- Over the quarter, the Fund's holding in US Equities decreased by 8.7% as funds were realised to invest in the Property portfolio.
- US and UK Equity Futures generated positive absolute returns, while Gilts generated a negative return.

# Appendix 1: Market Events

| Asset Class | What happened? Positive Factors | Negative Factors |
|---|---|---|
| **UK Equities** | ■ Business confidence, as measured by the Purchasing Managers Index (PMI), rose to 73.5 in December, its highest since March 2010. The PMI for the services sector stood at 58.8 in December, well above the 50 mark, separating growth from contraction.<br>■ The British Chamber of Commerce Quarterly Economic Survey, a major economic indicator closely watched by the Bank of England (BoE) and the Treasury upgraded its GDP growth forecast for 2014 to 2.7% in Q4 2013 from 2.2% in Q3 2013.<br>■ Unemployment fell more than expected in October to 7.4% (the lowest level since early 2009) from 7.6% a month earlier. The BoE has issued forward guidance indicating that interest rates are unlikely to increase above the current level of 0.5% until the unemployment rate falls to 7%. | ■ Equity dividends have enjoyed an impressive lead over bond yields for some time. However, with gilt yields now on an upward trajectory and investment grade bond yields also on the rise, UK equities might face some headwinds.<br>■ Britain's trade deficit, plus the losses UK plc. made on its overseas ventures, rose to GBP 21 billion in Q3 from a deficit of GBP 6 billion in the previous quarter. As a percentage of GDP, the deficit was 5.1%, the largest share in more than 20 years. |
| **Overseas Equities:** | | |
| **North America** | ■ The US Federal Reserve (Fed) announced that it will scale back its asset purchase programme from the current USD 85 billion per month to USD 75 billion per month beginning January 2014.<br>■ The Fed also signalled that if the employment and inflation environment remains stable, it expects similar monthly cutbacks over the course of 2014. This would lead to a formal end to the quantitative easing programme towards the fourth quarter of 2014.<br>■ GDP grew by a robust 3.6% (revised) in the fourth quarter, while the unemployment level fell to 7.0% by the end of November.<br>■ The US congress passed a budget deal aimed at rolling back sharp spending cuts, known as the sequester, over the next two years. This will reduce the likelihood of another government shutdown in the near term. | ■ The 10-year treasury yield (the benchmark interest rate) spiked over the 3% mark for the first time since July 2011 after the Fed’s announcement that it plans to taper its bond-buying program. Higher interest rates could increase the cost of borrowing for the corporates and jeopardise the nascent recovery in the economy.<br>■ Following a 30% rally in the S&P 500 through 2013, there is some concern that equity valuations appear unsustainable. |

| Asset Class | What happened? Positive Factors | What happened? Negative Factors |
|---|---|---|
| **Europe** | ■ The ECB surprised markets in November by cutting its main refinancing rate to a record low of 0.25%, and while it is not expected to cut the rate again, it is likely to flood the markets with another round of cheap cash early 2014.<br>■ Business activity in the Eurozone, as measured by the PMI, rose to 52.1 in December, recording the second-highest reading since mid-2011.<br>■ Ireland became the first country to exit the EU bailout programme without a precautionary credit line on December 15. | ■ The PMI for the services sector, which makes up a majority of the Eurozone's economy, dipped to 51.0 in December from 51.2 in November confounding expectations for a rise to 51.5. This indicated that growth in this sector has been weaker than anticipated.<br>■ Services firms cut prices again in the month of November, as they have done over the last two years, to facilitate business. The output price index rose to 48.6 from 47.9, still below the break-even mark. |
| **Japan** | ■ The Japanese economy grew at an annualised pace of 1.9% in Q3 2013, the fourth successive quarter of growth, lending more credibility to the expansionary monetary policy embarked upon by Prime Minister Shinzo Abe.<br>■ The government dropped the word 'Deflation' in its description of the economy for the first time in four years as core consumer inflation hit a five year high—past the halfway mark of the 2% target.<br>■ According to BOJ's quarterly survey, business confidence amongst large manufacturers surpassed expectations and rose from 12 points in Q3 to 16 points in Q4, the highest level since 2007, suggesting that economic prospects largely remain upbeat. | ■ Concerns remain over the ripple effects on the economy due to the proposed sales tax hike from the current 5% to 8% beginning April 2014.<br>■ The real wage scenario in the country could pose a serious challenge, as rising inflation coupled with less than desired wage increases will start to erode household spending power. |
| **Asia Pacific** | ■ South Korea recorded its 23rd consecutive month of trade surplus owing to strong exports, which grew by 2.2% year-on-year. This marked the highest level of annual exports in the country's history. | ■ Australia's GDP grew at an annualised rate of 2.3% in the third quarter of 2013, well below the consensus forecast of 2.6%. Economists argue that the nation needs to grow at a pace above 3% to curb the recent increases in the unemployment rate which currently stands at 5.7%. |

| Asset Class | What happened? Positive Factors | Negative Factors |
|---|---|---|
| **Emerging Markets** | ■ China, in its Third Plenum, announced sweeping reforms aimed at steering the nation from an investment-led developing nation to a consumption driven economy. The 60 point reform plan aims to achieve a sustainable growth and liberalise Chinese markets.<br>■ After weak performance through 2013, the emerging market space appears to be attractive from a valuation perspective.<br>■ China edged out the United States as the biggest trader of goods in 2013 as the value of its imports and exports crossed the USD 4 trillion mark for the year. The change in the pecking order reflects China's growing dominance in global trade.<br>■ India's current account deficit fell to 1.2% from 5% a year ago as the government's efforts to curb exports of non-essential commodities, particularly gold, started to yield the desired results. | ■ In China, concerns grew over the domino effects of the ailments in the banking system as asset repurchase rates surged to record highs after a government official warned about possible bank failures in the coming year.<br>■ Taiwan cut its growth forecast for 2014 to 2.6%, down from its earlier projection of 3.4%, reflecting weak prospects for one of the most export-oriented economies in the region.<br>■ Most emerging market economies still face headwinds due to inflationary pressures and are raising interest rates to combat high prices. Brazil raised its interest rates for the sixth time since March 2012, while Indonesia raised interest rates to the highest level since 2009.<br>■ Brazil's GDP shrank in Q3 2013 by 0.5% due to worsening fiscal imbalances, higher than target inflation and rising interest rates in the economy. |
| **Gilts** | ■ UK's GDP expanded by 0.8% in the third quarter, the strongest reading in over three years. Meanwhile, the International Monetary Fund (IMF) significantly upgraded Britain's growth outlook to 1.4% in 2013 and 1.9% in 2014. | ■ Market interest rates are expected to rise much sooner than expected as the BoE has brought forward its forecast for a drop in the unemployment to 7% by around 18 months from what was previously expected. |
| **Index Linked Gilts** | ■ With limited supply of paper and investors continuing to seek inflation protection, demand for index-linked gilts remains high, thus supporting prices. | ■ UK inflation continued to decline, reaching 2.0% in December 2013, affecting returns on index-linked instruments.<br>■ In an environment where central banks are able to control inflation within a target range, there is a limited upside to the return expectations on these instruments. |
| **Corporate Bonds** | ■ Corporations continue to maintain healthy balance sheets. While, the relatively attractive yield from parts of the corporate bond market continue to attract investor interest. | ■ The corporate bond market still suffers from liquidity constraints while uncertainty looms over interest rate increases. |

| Asset Class | What happened? | |
|---|---|---|
| | **Positive Factors** | **Negative Factors** |
| **Property** | ■ In November 2013, the UK commercial property values registered their highest monthly gain since March 2010, marking seven consecutive months of rises in values.<br>■ Mortgage approvals in the UK rose to about a six-year high in November 2013. House prices are rising across the country with the fastest growth rate seen in London where prices are now 14% above their previous peak in 2007.<br>■ The Construction PMI hit 62.6 in November 2013—the highest reading since August 2007. | ■ According to the changes to the capital gains tax structure announced by the chancellor George Osborne, foreign owners will be required to pay tax on gains in value on the UK properties starting April 2015. This move may dampen overseas investor sentiment into UK property market. |

## Economic statistics

| | Quarter to 31 December 2013 | | | Year to 31 December 2013 | | |
|---|---|---|---|---|---|---|
| | UK | Europe[1] | US | UK | Europe[1] | US |
| **Real GDP growth** | 0.7% | n/a | 0.8% | 2.8% | n/a | 2.7% |
| **Unemployment rate** | 7.1% | 11.1%[4] | 6.7% | 7.1% | 11.1%[4] | 6.7% |
| **Previous** | *7.7%* | *11.1%* | *7.3%* | *7.7%* | *11.0%* | *7.8%* |
| **Inflation change[2]** | 0.5% | 0.2% | -0.5% | 2.0% | 0.9% | 1.5% |
| **Manufacturing Purchasing Managers' Index** | 57.3 | 52.7 | 57.0 | 57.3 | 52.7 | 57.0 |
| **Previous** | *56.7* | *51.1* | *56.2* | *51.4* | *47.5* | *50.7* |
| **Quantitative Easing / LTRO [3]** | £375bn | €1,018bn | $3,794bn | £375bn | €1,018bn | $3,794bn |
| **Previous** | *£375bn* | *€1,018bn* | *$3,539bn* | *£375bn* | *€1,018bn* | *$2,774bn* |

Source: Thomson Reuters, market, Institute for Supply Management, Eurostat, United States Department of Labor, US Bureau of Economic Analysis. All figures to 31 December 2013 unless otherwise stated. "Previous" relates to data as at the previous quarter or year end.

(1) 15 Country Euro area; (2) CPI inflation measure; (3) Refers to amounts announced and therefore ignores changes due to debt maturing. LTRO refers to the European Central Bank's Long Term Refinancing Operation; (4) As at Nov 2013.

# Appendix 2: Glossary of Terms

| Term | Definition |
|---|---|
| Absolute Return | The actual return, as opposed to the return relative to a benchmark. |
| Annualised | Figures expressed as applying to 1 year. |
| Bond Assets | Assets held in the expectation that they will exhibit a degree of sensitivity to yield changes. The value of a benefit payable to a pensioner is often calculated assuming the invested assets in respect of those liabilities achieve a return based on UK bonds. |
| Growth Assets | Assets held in the expectation that they will achieve more than the return on UK bonds. The value of a benefit payable to a non-pensioner is often calculated assuming the invested assets in respect of those liabilities achieve a return based on UK bonds plus a premium (for example, if holding equities an equity risk premium may be applied). The liabilities will still remain sensitive to yields although the Growth assets may not. |
| Duration | The weighted average time to payment of cashflows (in years), calculated by reference to the time and amount of each payment. It is a measure of the sensitivity of price/value to movements in yields. |
| Funded Liabilities | The value of benefits payable to members that can be paid from the existing assets of the plan (i.e. those liabilities that have assets available to meet them). |
| High Yield | A type of bond which has a lower credit rating than traditional investment grade corporate bonds or government bonds. These bonds pay a higher yield than investment grade bonds. |
| Market Statistics Indices | The following indices are used for asset returns:<br>UK Equities: FTSE All-Share Index<br>Overseas Equities: FTSE AW All-World ex UK<br>UK Gilts (>15 yrs or >20 yrs): FTSE Brit Govt Fixed Over 15 (or 20) Years Index<br>Corporate Bonds(>15 yrs AA): iBoxx £ Corp 15+ Years AA Index<br>Non-Gilts (>15 yrs): iBoxx £ Non-Gilts 15+ Years Index<br>Index Linked Gilts (>5yrs): FTSE Brit Govt Index Link Over 5 Years Index<br>Hedge Funds: CS/Tremont Hedge Fund Index<br>Commodities: S&P GSCI Commodity GBP Total Return Index<br>High Yield: Bank Of America Merrill Lynch Global High Yield Index<br>Property: IPD Property Index (Monthly)<br>Cash: 7 day London Interbank Middle Rate<br>Price Inflation: All Items Retail Price Index<br>Earnings Inflation: UK Average Weekly Earnings Index - Whole Economy excluding Bonuses |
| Market Volatility | The impact of the assets producing returns different to those assumed within the actuarial valuation basis, excluding the yield change and inflation impact. |

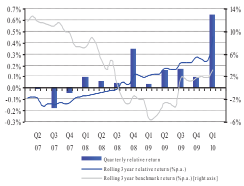
| Term | Definition |
|---|---|
| Mercer Gilt Yield | An estimate of the yield available on a notional portfolio of UK Government conventional gilt stocks whose cashflows approximately match the Fund's estimated benefit cashflows |
| Money-Weighted Rate of Return | The rate of return on an investment including the amount and timing of cashflows. |
| Non-Pensioner Liability | The value of benefits payable to those who are yet to retire, including active and deferred members. |
| Pensioner Liability | The value of benefits payable to those who have already retired, irrespective of their age. |
| Relative Return | The return on a fund compared to the return on another fund, index or benchmark. For IMAGE purposes this is defined as: Return on Fund less Return on Index or Benchmark. |
| Scheme Investments | Refers only to the invested assets, including cash, held by your investment managers. |
| Surplus/Deficit | The estimated funding position of the Scheme. This is not an actuarial valuation and is based on estimated changes in liabilities as a result of bond yield changes, asset movements and, if carried out, output from an asset liability investigation (ALI). If no ALI has been undertaken the estimate is less robust. |
| Three-Year Return | The total return on the fund over a three year period expressed in percent per annum. |
| Time-Weighted Rate of Return | The rate of return on an investment removing the effect of the amount and timing of cashflows. |
| Unfunded Liabilities | The value of benefits payable to members that cannot be paid from the existing assets of the Scheme (i.e. those liabilities that have no physical assets available to meet them). These liabilities are effectively the deficit of the Scheme. |
| Yield (Gross Redemption Yield) | The return expected from a bond if held to maturity. It is calculated by finding the rate of return that equates the current market price to the value of future cashflows. |

# Appendix 3: Glossary of Charts

The following provides a description of the charts used in Section 6 and a brief description of their interpretation.

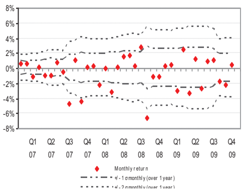
**Reference** **Description**

#1



This chart shows the quarterly relative return (blue bars) and rolling 3 year relative return (blue line) for the manager over 3 years/since inception. This shows the ability of the manager to achieve and outperform the benchmark over the medium term. The rolling 3 year benchmark absolute return (grey line) is overlaid to provide a context for relative performance, e.g. consistent underperformance in a falling market.

#2

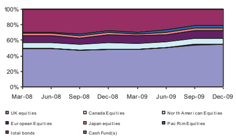


This chart shows the relative monthly returns for 3 years/since inception. It shows the level of fluctuation about the zero axis, i.e. the level of volatility of monthly returns and any tendency for positive or negative returns. The dotted lines show the standard deviation of returns over 1 year periods - this is a standard measure of risk which shows the magnitude of fluctuations of monthly returns. Under common **assumptions**, being within the inside dotted lines (i.e. 1 standard deviation) is roughly likely to occur 2/3rds of the time, while being within the outside lines is roughly likely to occur 1 in 20 times (i.e. 2 standard deviation - which is considered unlikely).

#4

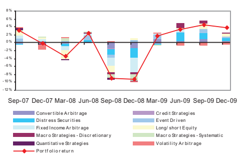
This chart shows the 3 year annualised tracking error (this is the standard deviation of returns which shows the magnitude of the fund returns compared to the benchmark) and the 3 year information ratio (this is the excess return divided by the tracking error). If tracking error increases, the risk taken away from the benchmark increases, and we would expect an increase in the excess return over time (albeit more variable). The turnover is provided to show if any increase in risk is reflected in an increase in the level of active management, i.e. purchases/sales in the portfolio.

#5



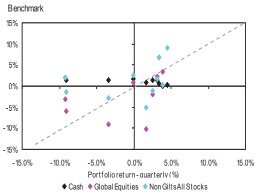
This chart shows the absolute asset allocation or hedge fund strategy allocation over time. This helps to identify any significant change or trends over time in allocation to particular asset allocations/hedge fund strategies.

#6



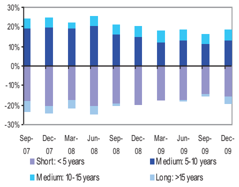
These charts show the breakdown of the return provided by each of the different hedge fund strategies or asset classes over time - this provides a profile of where the returns come from, and should be compared with the volatility chart above to see if risk taken is being rewarded accordingly. The total portfolio return is also shown.

#7



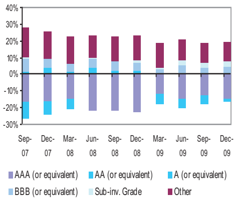

This chart plots the quarterly returns of the fund against quarterly returns of various indices. Any plots on the diagonal line represent the fund and the index achieving the same quarterly return - any below the line represents underperformance relative to the index, above the line represents outperformance. This is to highlight any apparent correlation between the fund returns and any particular index. If a fund is used as a diversifier from, say equities, we would expect to see a lack of returns plotted close to the diagonal line.

#8



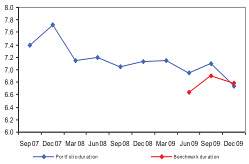

This chart shows the holding in short, medium and long maturity bonds relative to the benchmark. Over/underweight positions expose the fund to changes in the yield curve at different terms.

#9




This chart shows the holding in bonds with different credit ratings. AAA is the highest grading (usually for government or supranational organisation bonds) while below BBB is sub-investment grade and has a considerably higher risk of default. The lower the grade the higher the risk and therefore the higher the return expected on the bond.

#10



This chart shows the duration of the fund against the benchmark duration. It shows whether the fixed interest fund manager is taking duration bets against the benchmark.

# Appendix 4: Summary of Mandates

| Manager | Mandate | Benchmark | Outperformance target (p.a.) |
|---|---|---|---|
| Jupiter | UK Equities (Socially Responsible Investing) | FTSE All Share | +2% |
| TT International | UK Equities (Unconstrained) | FTSE All Share | +3-4% |
| Invesco | Global ex-UK Equities Enhanced (En. Indexation) | MSCI World ex UK NDR | +0.5% |
| Schroder | Global Equities (Unconstrained) | MSCI AC World Index Free | +4% |
| SSgA | Europe ex-UK Equities (Enhanced Indexation) | FTSE AW Europe ex UK | +0.5% |
| SSgA | Pacific inc. Japan Equities (Enhanced Indexation) | FTSE AW Dev Asia Pacific | +0.5% |
| Genesis | Emerging Market Equities | MSCI EM IMI TR | - |
| MAN | Fund of Hedge Funds | 3M LIBOR + 5.75% | - |
| Signet | Fund of Hedge Funds | 3M LIBOR + 3% | - |
| Stenham | Fund of Hedge Funds | 3M LIBOR + 3% | - |
| Gottex | Fund of Hedge Funds | 3M LIBOR + 3% | - |
| BlackRock | Passive Multi-asset | In line with customised benchmarks using monthly mean fund weights | 0% |
| BlackRock | Overseas Property | Customised benchmarks using monthly mean fund weights | 0% |
| RLAM | UK Corporate Bond Fund | iBoxx £ non-Gilts all maturities | +0.8% |
| Schroder | UK Property | IPD UK pooled | +1.0% |
| Partners | Global Property | IPD Global pooled | +2.0% |
| Cash | Internally Managed | 7 day LIBID | |

**JLT Employee Benefits**

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Bath & North East Somerset Council

## Access to Information Arrangements

## Exclusion of access by the public to Council meetings

| |
|---|
| Information Compliance Ref: LGA-0231-14 |

| |
|---|
| Meeting / Decision: AVON PENSION FUND INVESTMENT PANEL |
| Date: 26 February 2014 |

| |
|---|
| Author: Matt Betts |
| Report Title: Review Of Investment Performance For Periods Ending 31 December 2013<br><br>Exempt Appendix 3 – RAG Monitoring Summary Report<br>Exempt Appendix 4 - Emerging Markets Equity Fund - Update |

The Report contains exempt information, according to the categories set out in the Local Government Act 1972 (amended Schedule 12A). The relevant exemption is set out below.

| |
|---|
| Stating the exemption:<br>3. *Information relating to the financial or business affairs of any particular person (including the authority holding that information).* |

The public interest test has been applied, and it is concluded that the public interest in maintaining the exemption outweighs the public interest in disclosure at this time. It is therefore recommended that the Report be withheld from publication on the Council website. The paragraphs below set out the relevant public interest issues in this case.

<u>PUBLIC INTEREST TEST</u>

If the Committee wishes to consider a matter with press and public excluded, it must be satisfied on two matters.

Firstly, it must be satisfied that the information likely to be disclosed falls within one of the accepted categories of exempt information under the Local Government Act 1972. Paragraph 3 of the revised Schedule 12A of the 1972

Act exempts information which relates to the financial or business affairs of the organisations which is commercially sensitive to the organisations. The officer responsible for this item believes that this information falls within the exemption under paragraph 3 and this has been confirmed by the Council's Information Compliance Manager.

Secondly, it is necessary to weigh up the arguments for and against disclosure on public interest grounds. The main factor in favour of disclosure is that all possible Council information should be public and that increased openness about Council business allows the public and others affected by any decision the opportunity to participate in debates on important issues in their local area. Another factor in favour of disclosure is that the public and those affected by decisions should be entitled to see the basis on which decisions are reached.

Weighed against this is the fact that the exempt appendices contains the opinions of Council officers and Panel members. It would not be in the public interest if advisors and officers could not express in confidence opinions which are held in good faith and on the basis of the best information available.

The exempt appendices also contain details of the investment processes/strategies of the investment managers. The information to be discussed is commercially sensitive and if disclosed could prejudice the commercial interests of the investment managers.

It is also important that the Committee should be able to retain some degree of private thinking space while decisions are being made, in order to discuss openly and frankly the issues under discussion relating to the investment managers in order to make a decision which is in the best interests of the Fund's stakeholders.

The Council considers that the public interest has been served by the fact that a significant amount of information regarding the Investment Panel Activity has been made available – by way of the main report.

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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| Bath & North East Somerset Council | | |
|---|---|---|
| MEETING: | **AVON PENSION FUND INVESTMENT PANEL** | |
| MEETING DATE: | **26 FEBRUARY 2014** | **AGENDA ITEM NUMBER** **9** |
| TITLE: | **INFRASTRUCTURE TENDER PROCESS** | |
| WARD: | ALL | |
| **AN OPEN PUBLIC ITEM** | | |
| List of attachments to this report:<br>Appendix 1 – Agreed Infrastructure Policy Framework | | |

## 1 THE ISSUE

1.1 At their December 2013 meeting, the Committee agreed the framework for how the investment in infrastructure is to be structured, and agreed to delegate the tender process to Officers and Investment Adviser who will consult the Panel as required.

1.2 This paper updates the Panel on the proposed selection process, evaluation criteria and timescales for the Infrastructure tender.

## 2 RECOMMENDATION

**That the Panel**

2.1 **Agree the selection process and evaluation criteria for the Infrastructure tender process.**

2.2 **Select their preference for the selection panel makeup from section 6.4**

## 3 FINANCIAL IMPLICATIONS

3.1 There is provision in the budget for investment advice relating to investing in infrastructure.

## 4 BACKGROUND

4.1 The Fund's revised investment strategy agreed in March 2013 included a new allocation to Infrastructure of 5% of Fund assets.

4.2 An allocation to infrastructure meets the Fund's investment objectives as follows:

(1) Provides a source of returns as part of growth portfolio

(2) Reduces risk and increases diversification of returns within the investment portfolio

(3) Provides predictable income with a link to inflation

(4) Can generate income to meet the Fund's cashflow requirements

4.3 The framework agreed by Committee in their meeting on December 2013 identifies how the investment in infrastructure should be structured to best achieve these objectives.

## 5 MANDATE SPECIFICATION

5.1 The agreed framework defined a broad draft mandate specification and is shown in Appendix 1.

5.2 JLT have not sought to express more detailed guidelines on diversification requirements (by investment type, sector geography etc) in the mandate specification than those already stated in Appendix 1 as it is more appropriate to assess the diversification attributes provided by the managers in their tender submissions.

## 6 SELECTION PROCESS

6.1 As the investment will be made via pooled funds, OJEU requirements are not applicable. However, the Fund will apply the same level of rigour to the tender analysis and evaluation as would be employed for an OJEU process.

6.2 An open tender will be conducted (where all investment managers that express an interest will be invited to submit a bid). It should be noted that the nature of closed ended infrastructure funds means that they have periods where they are raising funds and do not accept investments once their fund is closed. This means that only the managers who are raising funds at the time of the tender will participate.

6.3 The Fund has commissioned its investment consultant, JLT, to manage the tender process. The tender will be managed through JLT's fully auditable online procurement portal. The process will be as follows:

(1) JLT develop tender questionnaire based on agreed mandate specification and evaluation criteria

(2) JLT issue open invite for all qualified organisations to submit a tender bid.

(3) JLT evaluate bids and draw up a long list report

(4) Following meeting on long list with officers, short list drawn up

(5) Officers and JLT do further due diligence on short listed managers

(6) Selection meeting to appoint from short listed managers

(7) Agree legals and implementation plan

6.4 It is expected that the process will take up to 6 months from advertising the tender until the investments begin with the successful tenderers. The process will begin with an invitation to tender in early March.

6.5 The selection meeting can be arranged as:

(1) A meeting of the full Panel (an extra meeting would be arranged);

or

(2) Delegate selection decision to a meeting of a selection panel including Officers, JLT and those members of the Panel who wish to attend

**Comments from the Panel on their preference will be sought at the meeting.**

6.6 Proposed dates for an all-day selection meeting to be held in Bath are as follows: Mon 16$^{th}$ June, Tues 17$^{th}$ June, Thurs 19$^{th}$ June, Fri 20$^{th}$ June

## 7 EVALUATION CRITERIA

7.1 The evaluation of the tenders will adhere strictly and transparently to the tender process. The following criteria will be used to evaluate each tender:

Philosophy, Investment Process and Portfolio Construction
Risk Controls
In-house systems and research
Performance (historic but also forward looking indicators of success)
Corporate Governance and Responsible Investment
Resources, team and client service
Corporate structure and business strategy
Fees

7.2 The tender questionnaire is designed to specifically address the above criteria and the evaluation will be based on the evidence put forward in the tender submissions.

7.3 Although the criteria is similar to previous searches (with a focus on process and portfolio construction, performance, risk controls, in-house systems and research), the following differences compared to previous search criteria highlight the different challenges of evaluating infrastructure managers/funds:

(1) Evaluation of performance - because of the nature of the asset type and the type of fund structure employed, it is less meaningful to assess performance data in isolation when comparing one manager with another due to differing characteristics such as vintage years, stage of investment and sector. Therefore the quantitative weighting, particularly in respect of past performance is reduced and a higher qualitative score is applied recognising

that a significant element of potential future performance is based on the sourcing of future deals and the analysis undertaken to assess projects.

(2) The evaluation of ESG - Evaluation of submissions includes a specific weighting to governance and socially responsible investment factors. However, environmental, social and governance factors will also be considered explicitly within the philosophy and portfolio construction sections. The investment process is expected to take account of potential risks (eg. reputation, regulatory) and opportunities, including but not limited to the construction process, materials used and ongoing operation of infrastructure assets.

(3) Slightly higher weighting to fees - because fees in this market are higher than average, a competitive fee basis should be appropriately rewarded. It should be noted that fees are more complex for this asset class than with others, often with performance fees and potentially hidden costs. The analysis will ensure transparency and fair comparison of costs across the different fee structures.

## 8 RISK MANAGEMENT

8.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

## 9 EQUALITIES

9.1 An equalities impact assessment is not necessary as the report contains only recommendations to note.

## 10 CONSULTATION

10.1 N/a

## 11 ISSUES TO CONSIDER IN REACHING THE DECISION

11.1 This report is for information only.

## 12 ADVICE SOUGHT

12.1 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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| **Contact person** | Liz Woodyard, Investments Manager 01225 395306 |
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**Infrastructure Policy Framework**

To meet the strategic objectives of the Fund, the proposed investment in infrastructure should incorporate the following characteristics:

(1) Target a return of gilts +2.5% p.a. net of fees, as set out in the SIP; (this is currently equivalent to a 7% return p.a. over the long term)

(2) Invest in an unlisted fund investing in unlisted infrastructure assets, based on the low correlation with equity markets and to take advantage of the illiquidity premium;

(3) Implement a global mandate giving the infrastructure manager the discretion to select where investments are made (geographically) to take advantage of all opportunities based on the risk/return characteristics of each deal. It is expected that the majority of exposure will be in developed markets and in core investments.

(4) Enable investment across core, value-add and opportunistic assets to ensure a steady and predictable yield whilst still meeting the return target of gilts +2.5%;

(5) Diversification across sectors to reduce sector concentration risk within the portfolio;

(6) Allow greenfield investments in addition to brownfield in order to meet return target of gilts +2.5% p.a.

(7) Allow debt to be considered under manager discretion for effective risk management of the portfolio

(8) No leverage at the fund level to enhance returns (accepting that a small amount of leverage maybe required over short term periods for operational reasons). Evaluate whether an appropriate limit on use of leverage in underlying investments is necessary or indeed feasible (especially if investing via pooled funds).

(9) Preference for one manager to manage the whole allocation but retain flexibility to appoint two managers if this is necessary to achieve the spread of investments needed to meet strategic aims. Invest in either in a direct fund structure or a fund of funds structure

The tender process will evaluate how each manager manages the various risks associated with infrastructure investing including financial (for example leverage), ESG, regulatory, and reputational risks, as well as how they select investments and allocate geographically.

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| MEETING: | **AVON PENSION FUND INVESTMENT PANEL** | |
| MEETING DATE: | **26 FEBRUARY 2014** | **AGENDA ITEM NUMBER** |
| TITLE: | **HEDGE FUND REVIEW - SCOPE** | |
| WARD: | ALL | |
| **AN OPEN PUBLIC ITEM** | | |
| List of attachments to this report:<br>Nil | | |

## 1 THE ISSUE

1.1 In response to a mixed performance within the Fund's hedge fund portfolio and to changes within the Fund's fund of hedge fund managers and the hedge fund industry as a whole, the Panel will review the Fund's current allocation to hedge funds and how the required exposure is achieved.

1.2 This paper describes the proposed aims and scope of the review, for agreement by the Panel.

## 2 RECOMMENDATION

**That the Panel**

2.1 **Agrees the scope for the Review of Hedge Fund Investments as set out in section 5.**

## 3 FINANCIAL IMPLICATIONS

3.1 There is provision in the 2014/15 budget for investment advice relating to the review of the Fund's hedge fund investments.

## 4 BACKGROUND

4.1 In the strategic review in 2013, the strategic target allocation to hedge funds was cut from 10% to 5%, with a permissible range of 0% to 7.5%

4.2 The pace of change within the Fund of Hedge Fund (FOHF) industry continues unabated. In response to falling Assets under Management and lower margins (as investor behaviour has changed, and fee levels have come under pressure), managers have reacted by consolidating and making changes to the structure of their business models.

4.3 Performance of the Hedge Fund 'sector' as a whole has historically underperformed strategic assumptions over the period the Fund has been invested. Individual managers have also underperformed their benchmarks to varying degrees. The review will update expectations for performance as a 'sector', and also for each manager we are currently invested with.

4.4 The Fund's current holding in FoHFs is as follows:

| **Fund** | **Holding** | **% of Total Fund** |
|---|---|---|
| Gottex | £57m | 1.7% |
| Signet | £66m | 2.0% |
| Stenham | £38m | 1.1% |
| **Total** | **£161m** | **4.9%** |

4.5 When the Fund first invested in hedge funds in 2007, it decided to invest via a Fund of Funds structure in order to get real diversification across managers and strategies and to use specialist expertise in the selection and monitoring of funds given that it was a new asset class for the Fund.

## 5 REVIEW OBJECTIVES AND SCOPE

5.1 The headline objectives of the review are as follows:

(1) To review the current allocation and determine whether any tactical change from the 5% central target is appropriate within the established strategic range of 0%-7.5% (which will remain unchanged)

(2) To review how best to get the required exposure (i.e. how the portfolio is structured and the best 'method of access')

5.2 The review will be undertaken by JLT, who will produce a report to meet the objectives. The report will include:

(1) Sector update - A description of how the hedge fund industry has evolved over time, how risks and opportunities have developed and an analysis of

the different options for how hedge fund investments can be accessed (for example through fund of funds, single funds, direct, bespoke funds)

(2) Performance assumptions – State how returns have compared to strategic assumptions and what implications this has for any changes to the tactical allocation. Compare absolute returns to those of other growth assets (equities mainly). Assess whether there are any significant differences between FoHF, single multi strategy and single strategy in performance and volatility or whether it depends more on the strategy they pursue.

(3) Performance of APF's FoHF managers versus benchmarks and strategic assumptions and whether there are any performance concerns with any of the managers

(4) Options for portfolio – Identify potential options, for example remain in FOHFs (retain some or all of current portfolio and/or select new FoHF manager(s)), go down a single multi strategy manager, or single strategy manager. Outline the different risks and costs involved including manager selection, diversification, and fee levels.

(5) Implementation considerations

5.3 JLT will make the following recommendations:

(1) What the target tactical allocation should be (within strategic range of 0%-7.5%)

(2) How best to structure that exposure.

(3) Any implications for implementing the recommendations

## 6 RISK MANAGEMENT

6.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

## 7 EQUALITIES

7.1 An equalities impact assessment is not necessary as the report contains only recommendations to note.

## 8 CONSULTATION

8.1 N/a

## 9 ISSUES TO CONSIDER IN REACHING THE DECISION

9.1 This report is for information only.

## 10 ADVICE SOUGHT

10.1 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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| MEETING: | **AVON PENSION FUND INVESTMENT PANEL** | |
| MEETING DATE: | **26 FEBRUARY 2014** | **AGENDA ITEM NUMBER** |
| TITLE: | **WORKPLAN** | |
| WARD: | ALL | |
| **AN OPEN PUBLIC ITEM** | | |
| List of attachments to this report: Nil | | |

## 1 THE ISSUE

1.1 This report sets out the workplan for the Panel to November 2014. The workplan is provisional as the Panel will respond to issues as they arise and as work is delegated from the Committee. The workplan over this period will largely consist of projects arising from the recent changes to the Investment Strategy.

1.2 The workplan will be updated for each Panel meeting and reported to the Committee.

## 2 RECOMMENDATION

**That the Panel:**

2.1 **Note the workplan to be included in Committee papers.**

2.2 **Notes the proposed manager meeting schedule for the Panel.**

## 3 FINANCIAL IMPLICATIONS

3.1 There are no financial implications arising from this report. Costs for meeting managers are provided for in the budget.

## 4 PROVISIONAL WORKPLAN

4.1 The provisional workplan is as follows:

| Panel meeting / workshop | Proposed reports |
|---|---|
| 26 February 2014 | • Review mangers performance to December 2013<br>• Infrastructure Policy<br>• Scope of hedge fund review<br>• Meet the managers workshop (Gottex, Signet) |
| 4 June 2014 | • Review mangers performance to March 2014<br>• Review of Hedge Funds<br>• Meet the managers workshop (Stenham, Schroder Property) |
| 3 September 2014 | • Review mangers performance to June 2014<br>• Meet the managers workshop (Schroder Equity, Record) |
| 21 November 2014 | • Review mangers performance to September 2014<br>• Meet the managers workshop (Jupiter, TT, Partners) |

4.2 The Panel's workplan will be included in the regular committee report setting out the committee's and pensions section workplans. This will enable the Committee to alter the planned work of the Panel.

## 5 PROPOSED MANAGER MEETING SCHEDULE

5.1 Following the agreement that each Manager should present to the Investment Panel once every 24 months the below proposed meeting schedule has been formulated.

5.2 The schedule has been designed to bring managers to the Panel that have not attended in more recent times. Where issues arise with particular managers, meeting will be incorporated into the schedule where necessary. In the case of the newly appointed Barings, Pyrford and Unigestion the first attendance at Panel is planned to occur within the 2 year period after investment. The proposed new Infrastructure manager will also be included in the meeting schedule going forward.

5.3 The proposed meeting schedule is as follows:

February 2014 – Signet & Gottex
June 2014 – Stenham & Schroder Property
September 2014 – Schroder Equity & Record Currency Management
November 2014 – Jupiter, TT & Partners
February 2015 – Genesis & RLAM
June 2015 – Invesco & SSgA
September 2015 – Pyrford & Barings

November 2015 – BlackRock & Unigestion

## 6 RISK MANAGEMENT

6.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

## 7 EQUALITIES

7.1 An equalities impact assessment is not necessary as the report contains only recommendations to note.

## 8 CONSULTATION

8.1 N/a

## 9 ISSUES TO CONSIDER IN REACHING THE DECISION

9.1 This report is for information only.

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10.1 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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