

## Bath & North East Somerset Council

MEETING:	<b>AVON PENSION FUND INVESTMENT PANEL</b>	
MEETING DATE:	<b>5 SEPTEMBER 2016</b>	<b>AGENDA ITEM NUMBER</b>
TITLE:	<b>Review Of Investment Performance For Periods Ending 30 June 2016</b>	
WARD:	<b>ALL</b>	
<b>AN OPEN PUBLIC ITEM</b>		
List of attachments to this report: Appendix 1 – Fund Valuation Appendix 2 – Mercer performance monitoring report (Panel version) Exempt Appendix 3 – RAG Monitoring Summary Report Appendix 4 – Mercer: Rationale for Currency Hedging Policy Appendix 5 – Mercer: Brexit Implications Discussion		

### **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 period ending 30 June 2016.
- 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 23 September 2016.
- 1.3 This is the first quarter that performance measurement has been provided by BNY Mellon, the Fund's custodian. The former provider, SSGA (WM Performance Services) withdrew from providing this service to non-custody clients at the end of 1Q16.

### **2 RECOMMENDATION**

**That the Investment Panel:**

- 2.1 **Notes the information as set out in the reports.**
- 2.2 **Identifies any issues to be notified to the Committee.**

### **3 FINANCIAL IMPLICATIONS**

- 3.1 The returns achieved by the Fund for the three years commencing 1 April 2016 will impact the next triennial valuation which will be calculated as at 31 March 2019. The returns quoted are net of investment management fees.

### **4 INVESTMENT PERFORMANCE**

#### **A – Fund Performance**

- 4.1 The Fund's assets increased by £160m (c. 4.2%) in the quarter ending 30 June 2016 giving a value for the investment Fund of £3,898m. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers.
- 4.2 Developed market equities delivered modest positive returns over the quarter on a local currency basis. Japanese equities were the main exception to this trend, falling by more than 7%. European equities (ex-UK) posted small negative returns and in the UK there was a marked difference between domestically focused small- and mid-cap stocks and global large cap stocks, with the FTSE100 returning 6.5% over the quarter. Emerging markets performed well through the quarter where Latin America in particular benefited from positive political developments in Brazil and Peru. Bond yields fell across all maturities over the quarter leading to positive returns from Gilts. There was an exceptional level of volatility in financial markets as a result of the EU referendum. On the day of the referendum, 10 year UK gilt yields fell by 0.30%, the largest one day move since the financial crisis. Corporate bonds benefitted from the decline in government bond yields and contributed a positive performance over the quarter (+4.2%).
- 4.3 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 23 September 2016.

#### **B – Investment Manager Performance**

- 4.4 A detailed report on the performance of each investment manager has been produced by Mercer – see pages 26 to 46 of Appendix 2.
- 4.5 BlackRock, Genesis and SSgA (Europe and Pacific) are all outperforming their three year performance targets. Schroder global equity, Partners Group, Jupiter, Invesco and TT are underperforming their respective 3 year targets. This underperformance is due in part to the volatility experienced around the EU referendum date and strong performance from Q2 2013 dropping out of the reporting period – see Appendix 3. Schroder property and RLAM, although slightly under, are broadly in line with their performance target (note that Schroder Property have a 5 year performance target).
- 4.6 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. Schroder (global equity mandate), Partners Group, Jupiter, Invesco and TT have received amber ratings this quarter. There is an update on these managers in Exempt Appendix 3. Schroder (property mandate) has underperformed its target on a 3 year basis but is within accepted tolerance levels on a 5 year basis (which is the performance period set out in the

management agreement) so receives a green rating. Equally, RLAM's marginal underperformance allows it to retain its green rating.

## 5 INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

- 5.1 **Asset Class Returns:** Returns from developed equities, index linked gilts, gilts and property outperformed the strategic assumptions over three years, the latter two were significantly ahead of the assumed return. Corporate bond returns are now also ahead of the strategic assumed return, following a strong Q2. Emerging market equities improved on last quarter due to strong performance throughout Q2 but continue to underperform the 3 year strategic assumption. Hedge funds underperformed significantly.
- 5.2 **Infrastructure:** \$195m of the Fund's \$300m commitment to infrastructure was drawdown in the fund managed by IFM on 1<sup>st</sup> April.
- 5.3 **Currency Hedging:** Since the result of the EU referendum, Sterling has fallen significantly against other major currencies (increasing the local market value of non-sterling assets). However, the currency hedge on the non-sterling assets has detracted from local currency returns on the four mandates that are hedged. Mercer expects currency volatility to continue and have reaffirmed their position on the appropriateness of a passive currency hedging strategy - see Appendix 4.
- 5.4 **Cash Management:** £60m of holdings in the corporate bond portfolio were sold down in July to fund currency hedging cash requirements necessary to maintain a 50% passive hedge level. Surplus proceeds from this sale will be held at Custody level in anticipation of further drawdowns from IFM (infrastructure mandate).
- 5.5 **Rebalancing:** No additional rebalancing activity was undertaken during the quarter. As at 18 August there are no allocations outside the rebalancing ranges.
- 5.6 **Brexit Implications:** The impact of the EU referendum outcome on the Fund is considered in Appendix 5. The Fund's discount basis, liability management framework and currency hedging program are set against the backdrop of continued uncertainty in financial markets and where material risks to asset growth may not have been fully weighed.

## 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. 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.

## 7 EQUALITIES

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

## **8 CONSULTATION**

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

## **9 ISSUES TO CONSIDER IN REACHING THE DECISION**

9.1 The issues to consider are contained in the report.

## **10 ADVICE SOUGHT**

10.1 The Council's Section 151 Officer (Divisional Director – Business Support) has had the opportunity to input to this report and has cleared it for publication.

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<b>Background papers</b>	Data supplied by BNY Mellon Performance Measurement
<b>Please contact the report author if you need to access this report in an alternative format</b>	