

Bath & North East Somerset Council

MEETING:	AVON PENSION FUND INVESTMENT PANEL	
MEETING DATE:	4 SEPTEMBER 2017	AGENDA ITEM NUMBER
TITLE:	Review Of Investment Performance For Periods Ending 30 June 2017	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
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 Exempt Appendix 4 – Manager Selection Decision Exempt Appendix 5 – Liability Risk Management Framework update Exempt Appendix 6 – Mapping of investment mandates to BPP Portfolios		

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 2017.
- 1.2 The report focuses on the performance of the individual investment managers and the implementation of the investment strategy. The full performance report with aggregate investment and funding analysis will be reported to the Committee meeting on 22 September 2017.

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 £128m (c. 2.9%) in the quarter ending 30 June 2017 giving a value for the investment Fund of £4,495m. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers.
- 4.2 Global equity markets advanced in Q2 owing to strong corporate earnings and generally positive economic data, which supported gains. The UK equity market experienced volatility over the quarter, benefitting from strong company fundamentals for much of May and then reversing gains as a hung parliament materialised. US equities posted gains despite political uncertainty over the ability of the US administration to push through its fiscally expansive policies. European equities performed well on improving sentiment following the election of President Macron, but gains were capped as the European Central Bank indicated that they would soon begin to taper quantitative easing. Japanese equities increased on continued accommodative central bank policy. Emerging market equities benefited from the supportive global backdrop, outperforming developed markets although this performance was not reflected in the Fund's emerging market mandates. Russia was the largest detractor to emerging market gains amid a sharp decline in Brent crude prices. In fixed income, bond yields rose sharply towards the end of June, as perceived 'hawkish' comments from the Bank of England and European Central Bank created expectations that monetary policy tightening might occur sooner than anticipated. Domestic inflation rose to 2.9% while wage growth remained low, placing further pressure on household spending. Over the quarter, sterling appreciated against the Dollar and the Yen but fell in value against the Euro.
- 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 22 September 2017.

B – Investment Manager Performance

- 4.4 A detailed report on the performance of each investment manager has been produced by Mercer – see pages 25 to 45 of Appendix 2.
- 4.5 All but one manager posted positive absolute returns over the quarter, reflective of wider market returns. The exception was Invesco who achieved -0.6% largely due to stock selection in May.
- 4.6 Relative returns were disappointing with the majority of managers underperforming their targets, on a 3 year rolling basis. Precise detail of amber rated managers can be found at Exempt Appendix 3.
- 4.7 Among the managers that are yet to reach the 3 year mark SLI recorded a positive absolute return of 1.2% over the three-months to 31 March 2017 compared to a target return of 1.4%. JP Morgan achieved a quarterly absolute return of 0.5% in USD terms and IFM posted 12.2% net IRR since inception, again in local currency terms.

4.8 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.

5 INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

5.1 **Asset Class Returns versus Strategic Assumptions:** All asset classes with the exception of hedge funds are materially ahead on a 3 year basis of the assumed strategic returns from the 2017 investment review. Index returns from developed and emerging equities, index-linked gilts, property and infrastructure are significantly ahead of their assumed strategic returns on a 3 year basis. Hedge funds remain below long-term averages due in part to exceptionally low cash rates.

5.2 **Risk Management Framework:** In November the Panel delegated the setting of the trigger levels to Officers in consultation with the Investment Consultant, Actuary and Manager. It was resolved that at time of implementation Panel members should be notified when triggers were either changed or activated. Since inception of the mandate a number of triggers have been activated and Exempt Appendix 5 serves to update members on what activity has taken place.

5.3 **Manager Selection Update:** At the 5 July Special Committee Meeting it was resolved to delegate the selection of a new Diversified Growth Fund and a Multi Asset Credit Fund to Officers in consultation with Mercer to meet the requirements of the recommended changes to the Investment Strategy. Details of the selection process and appointments made can be found at Exempt Appendix 4.

5.4 **MIFID II:** In July the FCA released details of the revised criteria that LGPS schemes would have to fulfil in order to opt up to 'professional investor' status from the default position of 'retail investor'. Concessions include a quantitative limb with a revised minimum portfolio size (£10m) and an additional criterion allowing 'opt up' providing the Fund in question complies with LGPS regulations for administrative business. The qualitative limb more appropriately takes account of LGPS governance structures and permits firms to take a collective view of the expertise possessed by Committee, Officers and the Consultant. The LGA have been working with the Investment Association to draft a template to be completed by LGPS schemes and submitted to investment managers by October 2017 in order to meet compliance by 3 January 2018.

5.5 **Currency Hedging:** Over the quarter, sterling appreciated c. 3.9% against the USD and c. 4.7% against the Yen, largely as a result of strong underlying fundamentals. The USD struggled on political rhetoric and central bank policy. The impact of the currency hedging overlay on Fund performance will be reported to the Committee on 22 September 2017. From January 2018 currency hedging contracts within the EU will be subject to daily exchange of variation margin under EMIR (European Market Infrastructure Regulation). This will mean that additional collateral needs to be held as part of the currency hedging programme. The Fund intends to maintain a larger cash holding in anticipation of having to meet its obligations under EMIR.

5.6 **Cash Management:** In April the Fund received deficit prepayments from some employers. On advice from Mercer this has been placed in cash liquidity funds in the short-term, and will be reviewed on an ongoing basis.

5.7 **Rebalancing:** As at 9th August all asset allocations, with the exception of an overweight cash position, remain within the acceptable range requiring no rebalancing action. Officers did not undertake any rebalancing activity during the quarter.

6 MAPPING OF CURRENT MANDATES TO BPP PORTFOLIOS

6.1 With BPP Ltd. now established and recruitment for staff now underway, the Client Group will begin to focus on the transition plan. The pool previously agreed the investment criteria for a range of portfolios, designed to enable each fund’s investment strategy to be delivered by BPP. These portfolios will now be reviewed to ensure all changes to fund strategies are accommodated.

6.2 Exempt Appendix 6 shows the current BPP portfolios and how the Fund’s current mandates map to these portfolios. The mapping takes into account immediate asset allocation changes post the 2017 investment review.

7 RISK MANAGEMENT

7.1 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.

8 EQUALITIES

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

9 CONSULTATION

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

10 ISSUES TO CONSIDER IN REACHING THE DECISION

10.1 The issues to consider are contained in the report.

11 ADVICE SOUGHT

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

