

London Borough of Merton Pension Fund Advisory Committee

Date: 28th September 2016

Agenda item: 3

Wards: All

Subject: Performance of the Pension Fund for the Quarter Ending June 2016

Lead officer: Caroline Holland Director of Corporate Services

Lead member: Councillor Imran Uddin

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RECOMMENDATION

- (a) Members are asked to note the content of this report, in particular, the market values and performance of the total fund and component portfolios for the quarter ending 30 June 2016, attribution of the results and the market environment during the period.
- (b) Members are asked to note that UBS Asset Management have been invited to attend this meeting to give a presentation to the Committee covering all three mandates (active global equity, passive equity and property) that they manage for the Pension Fund.

1.0 PURPOSE OF REPORT

- 1.1 To report the investment performance at total fund level, and of the individual fund managers, for the quarter to 30 June 2016.
- 1.2 The report gives the Committee a consistent basis on which to review the performance of the Fund as at 30 June 2016 and provide information to support future actions including periodic rebalancing and review of investment strategy and investment management arrangement.

2.0 PERFORMANCE REPORT

- 2.1 The attached Fund Analysis & Performance Report (**Appendix 1**) produced by WM Performance Services provides useful analysis and insights to the Pension Fund activity and results for the quarter to 30 June 2016.
- 2.2 The report highlights the performance of the total Fund by asset class compared to the customised benchmark. It also includes comprehensive analysis of the performance of each manager against their specific benchmark and a comparison of performance over longer periods.
- 2.3 At 30 June 2016 the total Fund was valued at £566.9m up by £38.1m (or 7.2%) since 31 March 2016.

3.0 MARKET BACKGROUND/OUTLOOK

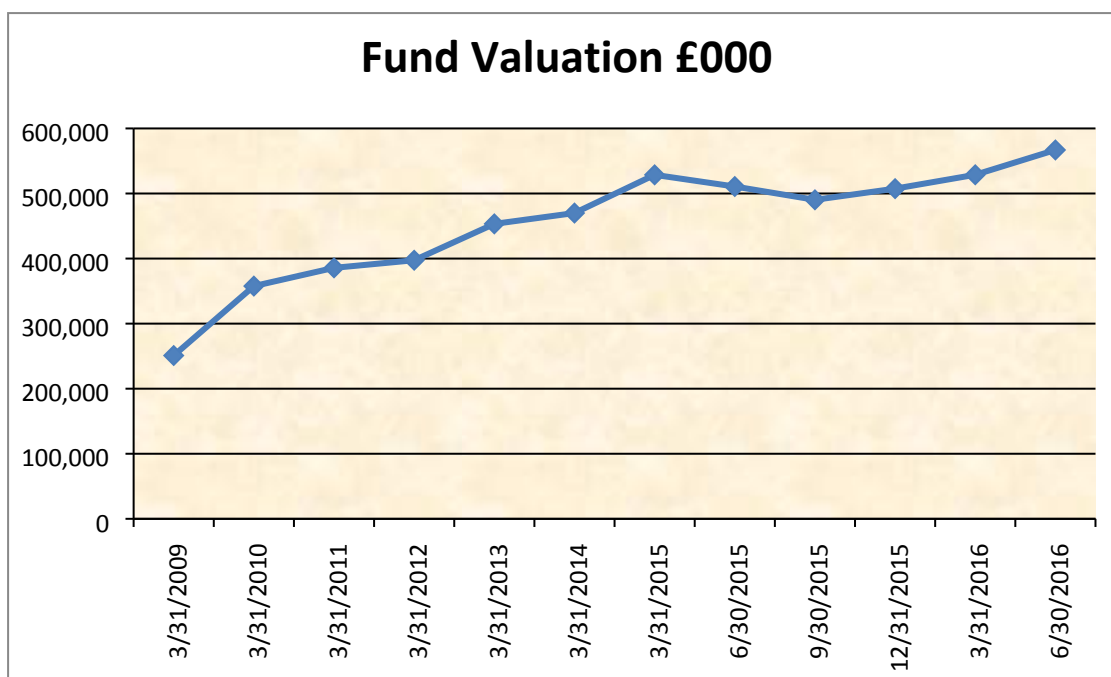
- 3.1 Volatility returned to investment markets late in the quarter when it emerged the United Kingdom had voted to leave the European Union in the Referendum on 23rd June 2016. Leading up to the vote, markets rallied on high expectation of a 'Remain' vote. Therefore, the 'Leave' result came as a shock to the markets, including the resignation of the Prime Minister and leader of the Remain campaign, David Cameron. Markets reacted negatively and Sterling suffered a significant drop in value against US dollar and Japanese Yen. However, equity markets finished the quarter strongly buoyed by good set of economic data; but government bond yields fell to record lows as markets began to price in the likelihood of further central bank action to boost economic activity.
- 3.2 Global markets continue to watch the US Fed closely. The recent dovish stance adopted by the Fed provided a welcome boost just as a number of other central banks remaining accommodative in light of weak growth.

4.0 PERFORMANCE OF THE FUND

- 4.1 The table below shows the Fund's strategic asset allocation as at 30 June 2016 against the benchmark allocation. The Fund was overweight Equity and underweight Bonds and Property compared to the benchmark.

At 30/06/2016	Total Equity %	Total Bonds %	Cash/Alts %	Property %	Total Fund %
Fund Asset Allocation	70.4	25.5	0.3	3.8	100.0
Fund Benchmark	69.4	25.9	N/A	4.7	100.0
Difference overweight / (underweight)	1.0	-0.4	N/A	-0.9	

- 4.2 The Fund outperformed the benchmark by 0.3% for the quarter ending 30 June 2016. It gained 7.2% compared to the benchmark return of 6.9% for the period. Year-to-date, the Fund outperformed the benchmark by 0.3%. The return for the year was 7.9% and 6.9% for the Fund and benchmark respectively.
- 4.3 The 0.3% outperformance was due wholly to asset allocation. The manager's results are discussed in more detail below in section 5.
- 4.4 The following graph illustrates the Fund's market value trend between 31 March 2009 and 30 June 2016. It shows that the market value of the Fund has appreciated by £316m or 126% over the 8 ¼ yr. period.



4.5 The table below shows the market value of each Portfolio at the start and end of the period. The change in value over the period is a combination of the net money flows into or out of each Portfolio and any gain or loss on the capital value of investments.

<i>Fund</i>	Market Value 31/03/16 £000	Capital Gain/loss £000	Income £000	Market Value 30/06/16 £000	% of Total Fund
UBS Passive Equity	226,073	12,957	1,196	240,318	42
Aberdeen Fixed Income	130,945	13,968	11	144,913	26
Aberdeen Active Equity	97,162	6,322	934	104,412	18
UBS Active Equity	52,694	1,804	645	55,208	10
UBS Property	15,184	-21	165	15,212	3
BlackRock Property	6,721	54	32	6,846	1
Total External Fund	528,779	35,085	2,982	566,908	100
Internal Investments	150			150	
Total	528,929			567,058	

4.6 The following table provides detailed analysis of the return on the Fund's investment for the period relative to the benchmark.

Sector	Market Value	Market Value	Fund Return	Benchmark
	Mar 2016 £000	June 2016 £000	June 2016 %	June 2016 %
UK Equities	221,842	236,199	5.3	4.7
Overseas Equities	153,461	162,460	8.0	8.0
• North America	53,664	57,330	10.2	10.3
• Continental Europe	41,507	43,709	4.9	4.4
• Total Far East	42,241	44,759	7.3	8.4
• Other Intl Equities	16,049	16,662	10.9	8.8
UK Bonds	32,682	35,952	9.9	10.1
Overseas Bonds	33,074	36,191	10.7	10.6
UK Index-Linked	65,173	72,769	11.1	11.1
Cash Alternatives	1,236	1,922	-0.2	
Property	21,312	21,416	1.2	0.1
Total	528,779	566,908	7.2	6.9

4.7 The Fund's assets are invested in various sectors and markets globally. During the quarter to June 2016, UK equities performed well which in contrast to the previous quarter made positive returns. Emerging markets again performed well.

5.0 FUND MANAGER PERFORMANCE

UBS

5.1 UBS manages three portfolios for LB Merton Pension Fund.

(1) UBS Active Global Equity

5.2 The market value of the active equity portfolio managed by UBS was £55.2m (£52.7m in March 2016). The portfolio return was 4.6% for the period, being below the benchmark return of 5.3%.

The table below shows the movement in the portfolio during the period.

UBS Active Equity	31/03//2016		Purchases £000	Sales £000	Gain/Loss £000	Income £000	30/06/2016	
	£000	%					£000	%
Total Equities	52,362	99	5,014	4,357	1,804	705	54,824	99
Cash & Cash Alternatives	332	1	5,068	5,016	0	0	384	1
Total	52,694	100	10,082	9,373	1,804	645	55,208	100

The manager's mandate is summarised in the following:

- For the portion of the Active Portfolio invested in UK Equities, the manager shall seek to outperform the benchmark by 1% p.a.
- For the portion of the Active Portfolio invested in Emerging Markets, the manager shall seek to outperform the benchmark by 2.0% p.a.

Performance of the UBS Active Equity over various time periods

<i>Period</i>	Manager %	Benchmark %	Variance %	Comment
Last 3 months	4.6	5.3	-0.7	underperformed
Last 12 months	0.2	2.4	-2.1	underperformed
Last 3 years	4.5	5.3	-0.8	underperformed
Last 5 years	5.2	5.7	-0.4	underperformed

(2) UBS Global Equity (Passive)

- 5.3 The passive equity portfolio was valued at £240.3m (£226.1m in March 2016). During the quarter the manager's performance of 6.3% was in-line with the benchmark of 6.3%.

The table below shows the movement of assets during the quarter.

<i>UBS Passive</i>	31/03/2016		Purchases £000	Sales £000	Gain/ Loss £000	Income £000	30/06/2016	
	£000	%					£000	%
UK Equities	124,104	55	6,363	2,966	4,626	1,225	132,127	55
North America	47,898	21	0	1,800	4,890	0	50,988	21
Continental Europe	26,942	12	0	0	1,161	0	28,104	12
Japan	13,438	6	0	200	1,185	0	14,423	6
Total Pacific (ex Japan)	14,180	6	0	300	1,095	0	14,975	6
Cash & Alternatives	-489	0	9,002	8,812	-1	1	-299	0
Total	226,073	100	15,366	14,078	12,957	1,196	240,318	100

The manager is to track the Benchmark index over rolling three year periods.

This table shows the performance of the portfolio.

Period	Manager %	Benchmark %	Variance %	Comment
Last 3 months	6.3	6.3	0	In line
Last 12 months	7.4	7.4	0	In line
Last 3 years	8.5	8.5	0	In line
Last 5 years	8.3	8.3	0	In line

(3) UBS Property Fund

- 5.4 The market value of the property portfolio managed by UBS was £15.2m (£15.2m in March 2016). The portfolio return was 1.0% during the quarter, compared to the benchmark return of 0.1%.

The table below shows the movement during the period within the portfolio.

UBS Triton (Property)	31/03//2016		Purchases	Sales	Gain/Loss	Income	30/06/2016	
	£000	%	£000	£000	£000	£000	£000	%
Property	14,591	96	0	0	-21	165	14,570	96
Cash & Cash Alternatives	593	4	136	88	0	0	642	4
Total	15,184	100	136	88	-21	165	15,212	100

The manager is to track the Benchmark index over rolling three year periods.

This table shows the performance of the portfolio.

Period	Manager	Benchmark	Variance	Comment
	%	%	%	
Last 3 months	1.0	0.1	0.9	outperformed
Last 12 months	8.4	7.2	1.2	outperformed
Last 3 years	14.0	12.5	1.5	outperformed
Last 5 years	6.6	8.4	-1.8	underperformed

Aberdeen Asset Management

- 5.5 Aberdeen manages two portfolios for the LB Pension Fund.

(1) Aberdeen Active Global Equity

- 5.6 The market value of the active equity portfolio managed by Aberdeen was £104.4m (£97.2m in March 2016). The portfolio return was 7.5% during the quarter, compared to the benchmark of 5.9%.

The table below shows the movement during the period within the portfolio.

Aberdeen Active Equity	31/03/2016		Purchases	Sales	Gain/Loss	Income	30/06/2016	
	£000	%					£000	£000
UK Equities	51,320	53	5,485	4,356	3,289	677	55,739	53
North America	5,766	6	0	0	576	1	6,342	6
Continental Europe	14,565	15	868	497	670	229	15,605	15
Japan	8,107	8	4,957	4,957	-14	23	8,093	8
Total Pacific (ex Japan)	6,517	7	0	0	751	33	7,268	7
Other Intl Equities	10,104	10	0	975	1,043	48	10,172	10
Cash & Alternatives	783	1	18,656	18,253	7	1	1,193	1
Total	97,162	100	29,966	29,038	6,322	934	104,412	100

- 5.7 Although this portfolio is an active mandate 35% is held in pooled funds. The Manager is required to outperform the benchmark by 1.25% p.a over rolling 3yr periods.

This table shows the performance of the portfolio

Period	Manager %	Benchmark %	Variance %	Comment
Last 3 months	7.5	5.9	1.6	outperformed
Last 12 months	4.1	4.9	-0.8	underperformed
Last 3 years	5.0	6.7	-1.7	underperformed
Last 5 years	6.6	6.2	0.4	outperformed

(2) Aberdeen (Bonds)

- 5.8 The market value of the bonds portfolio was £144.9m (£130.9m in March 2016). During the quarter the manager's performance of 10.7% was in-line with the benchmark of 10.7%.

The table below shows the movement during the period within the portfolio.

Aberdeen (Bonds)	31/03/2016		Purchases	Sales	Gain/Loss	Income	30/06/2016	
	£000	%					£000	£000
UK Bonds	32,682	25	306	261	3,224	10	35,952	25
Overseas Bonds	33,074	25	0	360	3,477	16	36,191	25
UK Index Linked	65,173	50	331	0	7,265	22	72,769	50
Cash & Alternatives	16	0	620	637	2	0	2	0
Total	130,945	100	1,258	1,258	13,968	11	144,913	100

The manager is required to outperform its benchmark by 0.60% p.a. over a rolling three year period.

This table shows the performance of the portfolio.

Period	Manager %	Benchmark %	Variance	Comment
Last 3 months	10.7	10.7	0	In line
Last 12 months	20.5	20.6	-0.1	underperformed
Last 3 years	11.1	11.3	-0.2	underperformed
Last 5 Years	9.6	10.0	-0.4	underperformed

BlackRock (Property)

- 5.9 The market value of the property portfolio managed by BlackRock was £6.8m (£6.7m in March 2016). The return on the portfolio was 1.3%, compared to benchmark return of 0.1%.

The following table below shows the movement in the portfolio during the period.

<i>Blackrock</i>	31/03/2013		Purchases £000	Sales £000	Gain/Loss £000	Income £000	30/06/2016	
	£000	%					£000	%
Property	6,721	100	70	0	54	45	6,846	100
Cash & Cash Alternatives	0	0	70	70	0	0	0	0
Total	6,721	100	141	70	54	32	6,846	100

The manager is required to outperform the average of similar institutional pooled vehicles by investing in a diversified range of property throughout the UK, principally, but not exclusively, in the retail, office and industrial/warehouse sectors.

This table shows the performance of the portfolio.

Period	Manager %	Benchmark %	Variance %	Comment
Last 3 months	1.3	0.1	1.2	outperformed
Last 12 months	6.7	7.2	-0.5	underperformed
Last 3 years	10.6	12.5	-1.9	underperformed

6. OTHER ISSUES AFFECTING THE FUND

- 6.1 Review of the pension fund investment strategy and investment management arrangements and triennial actuarial valuation are ongoing. A Pension Fund Business Plan and PFAC Work Programme are in place. The Pension Fund annual report and Accounts for 2015/16 has been audited.

7. FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS

7.1 All relevant implications are included in the report.

8. LEGAL AND STATUTORY IMPLICATIONS

8.1 All relevant implications are included in the report.

9. HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS

9.1 N/A

10. RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS

10.1 Risk management is an integral part of designing the investment portfolio of the fund particularly in the current volatile economic environment.

11. BACKGROUND PAPERS

11.1 StateStreet Analytics performance report and individual Fund Managers investment reports

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