

London Borough of Merton Pension Fund Advisory Committee

Date: 29th June 2016

Agenda item: 3

Wards: All

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

Lead officer: Caroline Holland Director of Corporate Services

Lead member: Councillor Imran Uddin

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RECOMMENDATION

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 31 March 2016, attribution of the results and the market environment during the period.

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 31 March 2016.
- 1.2 The report gives the Committee a consistent basis on which to review the performance of the Fund as at 31 March 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 of the Pension Fund activity and results for the quarter to 31 March 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 31 March 2016 the total Fund was valued at £528.8m up by £11.7m (or 2.2%) since 31 December 2016.

3.0 Market Background/Outlook

- 3.1 Markets had a turbulent start to 2016 as instability in China's domestic stock market, a further slump in oil prices and concerns over the impact of negative

interest rates led to an underperformance in risk-assets while core government bonds benefited from a ‘flight to safety’.

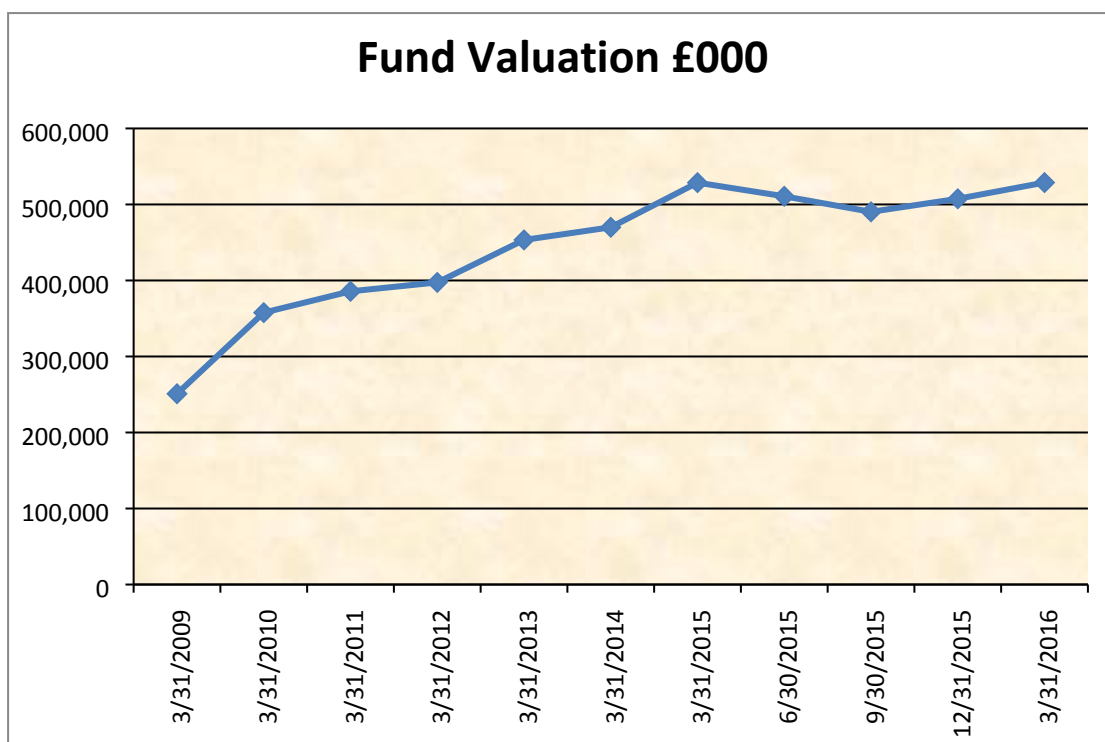
- 3.2 Upward momentum resumed in the final weeks of the quarter as the oil price recovered sharply and both the European Central Bank and the Bank of Japan committed to further monetary policy easing. An increasingly dovish tone from the Fed in the US, following the rate rise seen in December 2015, meant the US Dollar had its worst quarter in five years.

4.0 PERFORMANCE OF THE FUND

- 4.1 The table below shows the Fund’s strategic asset allocation as at 31 March 2016 against the asset allocation of the benchmark. The Fund was overweight Equity and underweight Bonds and Property compared to the benchmark.

At 31/03/2016	Total Equity %	Total Bonds %	Cash/Alts %	Property %	Total Fund %
Fund Asset Allocation	71.0	24.7	0.2	4.0	100.0
Fund Benchmark	68.9	26.2	N/A	4.9	100.0
Difference overweight / (underweight)	2.1	-1.5	N/A	-0.9	

- 4.2 The Fund underperformed the benchmark by 0.1% for the quarter ending 31 March 2016. It gained 2.3% compared to the benchmark return of 2.4% for the period. Year-to-date, the Fund underperformed the benchmark by 1.1%. The return for the year was -1.8% and -0.7% for the Fund and benchmark respectively.
- 4.3 The 0.1% underperformance 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 31 March 2016. It shows that the market value of the Fund has appreciated by £278m or 111% over the 8 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 31/12/15 £000	Capital Gain/loss £000	Income £000	Market Value 31/03/16 £000	% of Total Fund
UBS Passive Equity	219,227	1,259	559	226,073	43
Aberdeen Fixed Income	122,437	8,545	41	130,945	25
Aberdeen Active Equity	95,614	774	790	97,162	18
UBS Active Equity	52,892	-476	223	52,694	10
UBS Property	10,620	-20	120	15,184	3
BlackRock Property	6,662	14	29	6,721	1
Total External Fund	507,453	10,096	1,762	528,779	100
Internal Investments	9,580			150	0
Total	517,033			528,929	

4.6 The Fund's assets are invested in various sectors and markets globally. During the quarter to March 2016, emerging market equities performed well as did fixed income investments which in contrast to the previous quarter, yielded positive returns.

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

Sector	Market Value		Fund Return	Benchmark
	Dec 2015 £000	Mar 2016 £000	Mar 2016 %	Mar 2016 %
UK Equities	218,026	221,842	-0.3	-0.4
Overseas Equities	149,150	153,461	2.5	2.6
• North America	52,395	53,664	4.2	4.2
• Continental Europe	40,944	41,507	1.0	0.2
• Total Far East	40,755	42,241	-0.8	0.6
• Other Intl Equities	15,055	16,049	9.8	8.6
UK Bonds	30,640	32,682	6.9	6.9
Overseas Bonds	31,624	33,074	8.1	8.6
UK Index-Linked	60,163	65,173	6.6	6.5
Cash Alternatives	1,157	1,236	8.0	N/A
Property	16,693	21,312	0.9	1.1
Total	507,453	528,779	2.3	2.4

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 £52.7m (Dec 2015 £52.9m). The portfolio return was -0.5% for the period, being below the benchmark return of 0.7%.

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

UBS Active Equity	31/12//2015		Purchases	Sales	Gain/Loss	Income	31/03/2016	
	£000	%	£000	£000	£000	£000	£000	%
Total Equities	52,334	99	5,135	4,631	-476	282	52,362	99
Cash & Cash Alternatives	558	1	4,896	5,122	0	0	332	1
Total	52,892	100	10,031	9,753	-476	223	52,694	100

The manager's mandate is summarised below:

- 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	-0.5	0.7	-1.2	underperformed
Last 12 months	-4.2	-4.6	0.4	outperformed
Last 3 years	2.5	3.0	-0.5	underperformed
Last 5 years	4.4	4.8	-0.4	underperformed

(2) UBS Global Equity (Passive)

5.3 The passive equity portfolio was valued at £226.1m (£219.2m Dec 2015). During the quarter the manager's performance of 0.8% was slightly above the benchmark of 0.7%.

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

<i>UBS Passive</i>	31/12/2015		Purchases £000	Sales £000	Gain/ Loss £000	Income £000	31/03/2016	
	£000	%					£000	%
UK Equities	119,977	55	8,232	3,118	-987	586	124,104	55
North America	46,417	21	700	1,200	1,981	0	47,898	21
Continental Europe	26,093	12	775	0	74	0	26,942	12
Japan	14,038	6	0	0	-600	0	13,438	6
Total Pacific (ex Japan)	12,888	6	500	0	792	0	14,180	6
Cash & Alternatives	-186	0	16,637	16,940	0	1	-489	0
Total	219,227	100	26,844	21,257	1,259	559	226,073	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	0.8	0.7	0.1	outperformed
Last 12 months	-2.4	-2.4	-0.0	In line
Last 3 years	6.1	6.0	0.1	outperformed
Last 5 years	7.3	7.3	0.0	In line

(3) UBS Property Fund

- 5.4 The market value of the property portfolio managed by UBS was £15.2m (£10.6m in Dec 2015). The portfolio return was 0.7% during the quarter, compared to the benchmark return of 1.1%.

An additional commitment in the UBS Triton Trust of £4.6m was made in February 2016. This commitment was financed from 2015/16 additional LBM employer contributions.

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

<i>UBS Triton (Property)</i>	31/12//2015		Purchases	Sales	Gain/Loss	Income	31/03/2016	
	£000	%	£000	£000	£000	£000	£000	%
Property	10,031	94	4,581	0	-20	120	14,591	96
Cash & Cash Alternatives	589	6	4,671	4,668	0	0	593	4
Total	10,620	100	9,252	4,668	-20	120	15,184	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	0.7	1.1	-0.3	underperformed
Last 12 months	10.8	10.6	0.2	outperformed
Last 3 years	13.8	13.0	0.8	outperformed
Last 5 years	7.0	8.8	-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 £97.2m (Dec 2015 £95.6m). The portfolio return was 1.6% during the quarter, compared to the benchmark of 1.0%.

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

Aberdeen Active Equity	31/12/2015		Purchases	Sales	Gain/ Loss	Income	31/03/2016	
	£000	%					£000	£000
UK Equities	51,264	54	5,835	5,584	-195	581	51,320	53
North America	5,978	6	0	450	238	1	5,766	6
Continental Europe	14,851	16	1,119	1,643	238	99	14,565	15
Japan	8,059	8	800	0	-752	20	8,107	8
Total Pacific (ex Japan)	5,770	6	500	0	247	29	6,517	7
Other Intl Equities	9,505	10	0	400	998	49	10,104	10
Cash & Alternatives	186	0	9,810	9,213	0	88	783	1
Total	95,614	100	18,065	17,290	774	790	97,162	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	1.6	1.0	0.6	outperformed
Last 12 months	-6.8	-4.1	-2.7	underperformed
Last 3 years	1.8	4.1	-2.3	underperformed
Last 5 years	5.7	5.2	0.5	outperformed

(2) Aberdeen (Bonds)

5.8 The market value of the bonds portfolio was £130.9m (Dec 2015 £122.4m). The portfolio return was 7.0%, compared to the benchmark of 7.1%.

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

Aberdeen (Bonds)	31/12/2015		Purchases	Sales	Gain/ Loss	Income	31/03/2016	
	£000	%					£000	£000
UK Bonds	30,640	25	161	194	2,075	29	32,682	25
Overseas Bonds	31,624	26	0	1,010	2,460	16	33,074	25
UK Index Linked	60,163	49	1,009	0	4,001	34	65,173	50
Cash & Alternatives	9	0	1,167	1,169	9	0	16	0
Total	122,437	100	2,336	2,374	8,545	79	130,945	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	7.0	7.1	-0.1	underperformed
Last 12 months	3.3	3.6	-0.3	underperformed
Last 3 years	5.2	5.5	-0.3	underperformed
Last 5 Years	8.1	8.5	-0.4	underperformed

BlackRock (Property)

- 5.10 The market value of the property portfolio managed by Blackrock was £6.7m (Dec 2015 £6.7m). The return on the portfolio was 0.6%, compared to benchmark return of 1.1%.

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

<i>Blackrock</i>	31/12/2015		Purchases £000	Sales £000	Gain/Loss £000	Income £000	30/03/2016	
	£000	%					£000	%
Property	6,662	100	45	0	14	45	6,721	100
Cash & Cash Alternatives	0	0	45	45	0	0	0	0
Total	6,662	100	90	45	14	45	6,721	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	0.6	1.1	-0.5	underperformed
Last 12 months	7.7	10.6	-2.9	underperformed
Last 3 years	10.7	13.0	-2.3	underperformed

6. OTHER ISSUES AFFECTING THE FUND

- 6.1 Review of the pension fund investment strategy and investment management arrangements is proposed. A draft Pension Fund Business Plan and draft PFAC Work Programme are the subjects of separate reports to this meeting.

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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