

SURREY COUNTY COUNCIL

PENSION FUND BOARD

DATE: 14 FEBRUARY 2014

LEAD OFFICER: SHEILA LITTLE, CHIEF FINANCE OFFICER

SUBJECT: MANAGER ISSUES AND INVESTMENT PERFORMANCE



6

**SUMMARY OF ISSUE:**

This report is a summary of all manager issues that need to be brought to the attention of the Pension Fund Board, as well as manager investment performance.

**RECOMMENDATIONS:**

It is recommended that the Pension Fund Board:

1. approve the report and the decisions as laid out.
2. approve the purchase of an annual insurance policy with Legal & General to insure the fund against the cost of ill health retirements, subject to the County Council's Head of Procurement confirming that it is not necessary to formally tender for an insurance provider.

**REASON FOR RECOMMENDATIONS:**

In order to achieve best possible performance alongside optimal risk.

**DETAILS:****1) Manager Issues during the Quarter**

<b>Manager</b>	<b>Issue</b>	<b>Status/Action Required</b>
LGIM	Possible Rebalancing	Members are invited to discuss the question of rebalancing with the asset allocation being outside of the policy control limits. The asset allocation at 31 December 2013 and 31 January 2014 are shown in Annex 1.
Standard Life	P750 Fund	Members are invited to give consideration to the Standard Life P750 Fund.
Mirabaud	Client meeting	Update included in minutes of external fund manager meetings held on 4 February 2014.
Standard Life	Client meeting	Update included in minutes of external fund manager meetings held on 4 February 2014.
CBRE	Client meeting	Update included in minutes of external fund manager meetings held on 4 February 2014.
Newton	Client meeting	Update included in minutes of external fund manager meetings held on 4 February 2014.
Marathon	Presentation	Managers will be presenting at the Board meeting on 14 February 2014.

## 2) Freedom of Information Requests

The table below summarises the Freedom of Information request responses provided by the Fund during the last quarter.

<b>Date</b>	<b>Requestor</b>	<b>Organisation</b>	<b>Request</b>	<b>Response</b>
October	Company	Pitchbook	Information on private equity holdings	Provided summary as at 31 Mar 2013
November	Company	BBC	Details of all gifts and hospitality, expenses, foreign travel undertaken by fund director from April 2008 onwards.	A full response comprising all travel expenses and any hospitality offered or accepted during the period requested.

### 3) **Future Pension Fund Board Meetings/Pension Fund AGM**

The schedule of meetings for 2014 is as follows:

- 14 Feb 2014: Board meeting hosted at Axa Investment Management, London.
- 23 May 2014: Board meeting hosted at County Hall.
- 19 Sep 2014: Board meeting hosted at County Hall.
- 14 Nov 2014: Board meeting hosted at County Hall.
- 21 Nov 2014: Pension Fund Annual Meeting hosted at County Hall.

### 4) **Stock Lending**

The Fund began lending securities during November 2013 and in the period to 31 December 2013 earned a net income for the Fund of £24,382, with the average percentage of available securities on loan at 4.8% providing a gross yield of 0.019%.

### 5) **Share Voting**

The Strategic Manager will present a report at the Board meeting.

### 6) **Ill Health Insurance**

Members considered the Ill Health Insurance report dated 15 November 2013 at the last meeting. The report observed that now appeared to be an appropriate time to consider insuring against ill health retirement costs (Tier 1 and Tier 2) because individual cost of ill health retirements would increase with the new LGPS (improved 1/49 accrual rate) coming into effect in April 2014, while Legal & General had recently significantly reduced their premium rates from 0.85% to 0.63%. The report also observed that purchasing a policy on a whole fund basis would result in a lower premium for the entire membership and easier administration. Subject to approval from the Board, procurement advice would be sought from the Head of Procurement.

The report observed that the risk of ill health retirements was greater for smaller employers than for larger employers and the introduction of such an initiative would emphasise the paternalistic remit of the Pension Fund as a whole as well as the Pension Fund Board. The potential risk to the Pension Fund if small employers went out of business because of the cost of ill health retirements was emphasised.

The question of running an internal pooling arrangement to self-insure against ill health retirements was discussed. This would avoid the Fund being exposed to the profit element of the insurance business but possibly also expose the Fund to significant liability by taking on ill health risk. The pros and cons of self insurance are summarised:

**Pros**

- Benefit to the fund of a possible low claim environment
- Stability of employer contribution rate

**Cons**

- No transfer or reduction of risk exposed to the Fund
- Premiums set insufficient to meet total ill-health strain
- Risk remains with Fund that cost of ill-health retirements is higher than expected with the possibility of setting a higher premium than L&G to counter this
- Additional complex administration to notionally separate and invest the assets ring fenced to cover the pension strain costs

A detailed briefing note from Hymans Robertson is attached as Annex 2, providing more information on the ill health insurance issues.

Members are invited to discuss the proposal. The following options are available with the recommendation being to approve the purchase of an annual insurance policy with Legal & General to insure the fund against the cost of ill health retirements, subject to the County Council's Head of Procurement confirming that it is not necessary to formally tender for an insurance provider.

- a) Not to provide ill-health insurance.
- b) To provide ill-health insurance by means of the purchase of an ill-health insurance policy from Legal and General.
- c) To provide ill-health insurance by means of self-insurance.
- d) To permit fund employers to individually purchase an ill-health insurance policy from Legal and General.



## **Report of the Pension Fund & Treasury Manager**

### **Internally Managed Cash**

The internally managed cash balance of the Pension Fund was £3.8m as at 31 December. The Pension Fund repaid £2m of the £20m temporary loan from Surrey County Council on 31 December with the £18m balance repaid 22 January 2014. The fund has agreed two smaller short term loans at more attractive rates from other local authorities than would be available from the County: £5m from Coventry Council at 0.45% and £6m from Leicester Council at 0.40%. These will be repaid by mid March.

### **Private Equity Opportunities**

There are no opportunities to report this quarter.

### **Actuarial Update**

The triennial actuarial valuation as at 31 March 2013 is now complete. Officers have received an initial actuarial report that assessed the funding level at 31 March 2013 at 72.3%, up from 72.0% at 31 March 2010. The actuary's report is included in a separate report included on the Board meeting agenda.

The actuary made a presentation of his initial findings at the Board meeting on 15 November 2013 and also presented at the Pension Fund Annual Meeting on 22 November 2013.

The Pension Fund and Treasury Manager has been in regular contact with the Surrey Treasurers Association to keep them apprised of progress. A meeting for the Surrey District and Borough Councils was hosted at County Hall on 8 November 2013 with the actuary in attendance.

The Pension Fund and Treasury Manager has also liaised extensively with a significant number of the other employer organisations of the Surrey Pension Fund.

### **Governance Strategies and Policies**

All outstanding papers have now been drafted and presented to the Board, apart from the Pensions Administration Service Level Agreement. The final draft of the Pensions Administration Strategy is part of this meeting's agenda.

### **Fund Manager Meetings on 4 February 2014**

Notes of the fund manager meetings of 4 February 2014 are included as Annex 3.

## Report of the Pension Fund & Treasury Manager

### Financial and Performance Report

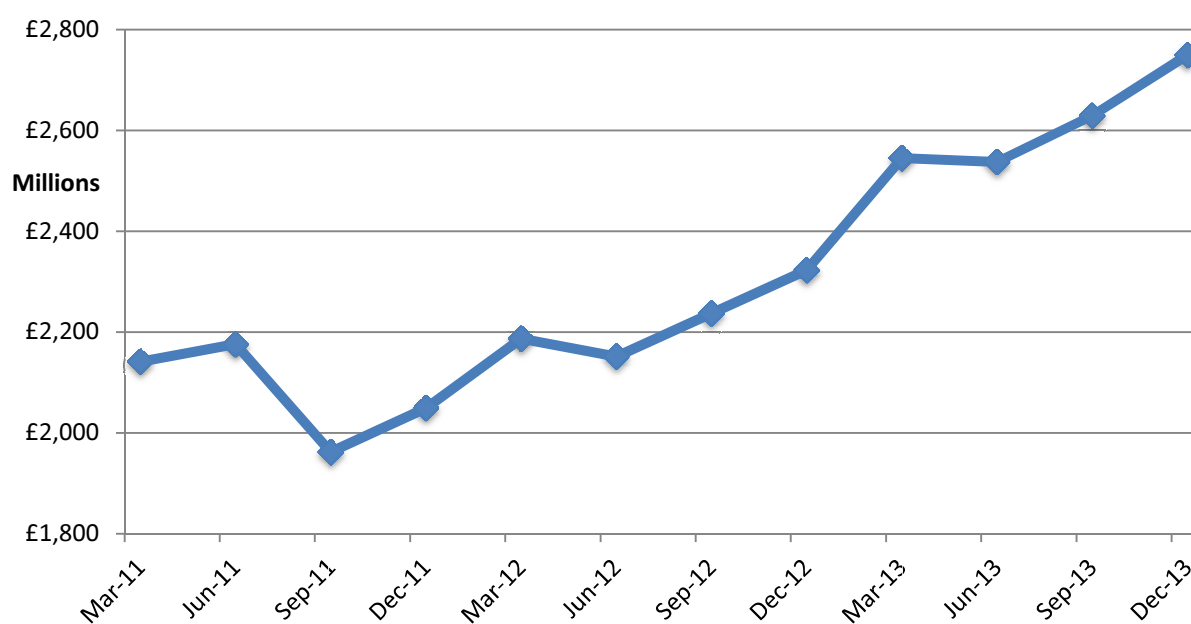
#### 1. Market Value

The value of the Fund was £2,749.5m at 31 December 2013 compared with £2,629.1m at 30 September 2013. Investment performance for the period was +4.4%.

The increase is attributed as follows:

	£m
<b>MARKET VALUE AT 30/09/2013</b>	<b>2,629.1</b>
Contributions less benefits and net transfer values	4.5
Investment income received	10.8
Investment expenses paid	-2.9
Market Movements	108.0
<b>Market Value at 31/12/2013</b>	<b>2,749.5</b>
<b>Estimated Market Value at 31/01/2014</b>	<b>2,727.1</b>

#### Total Fund Value

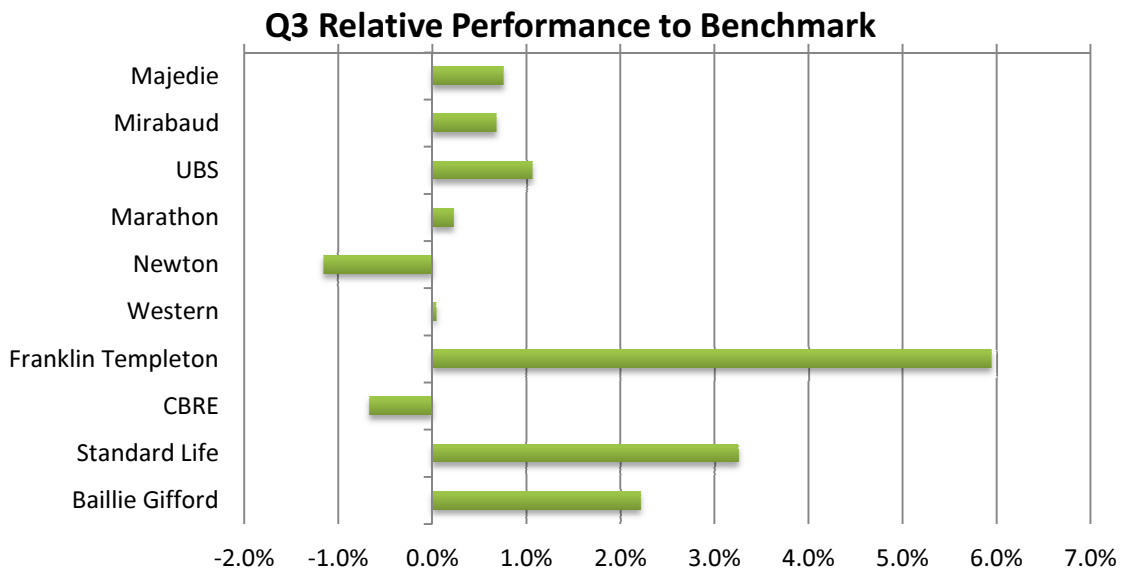
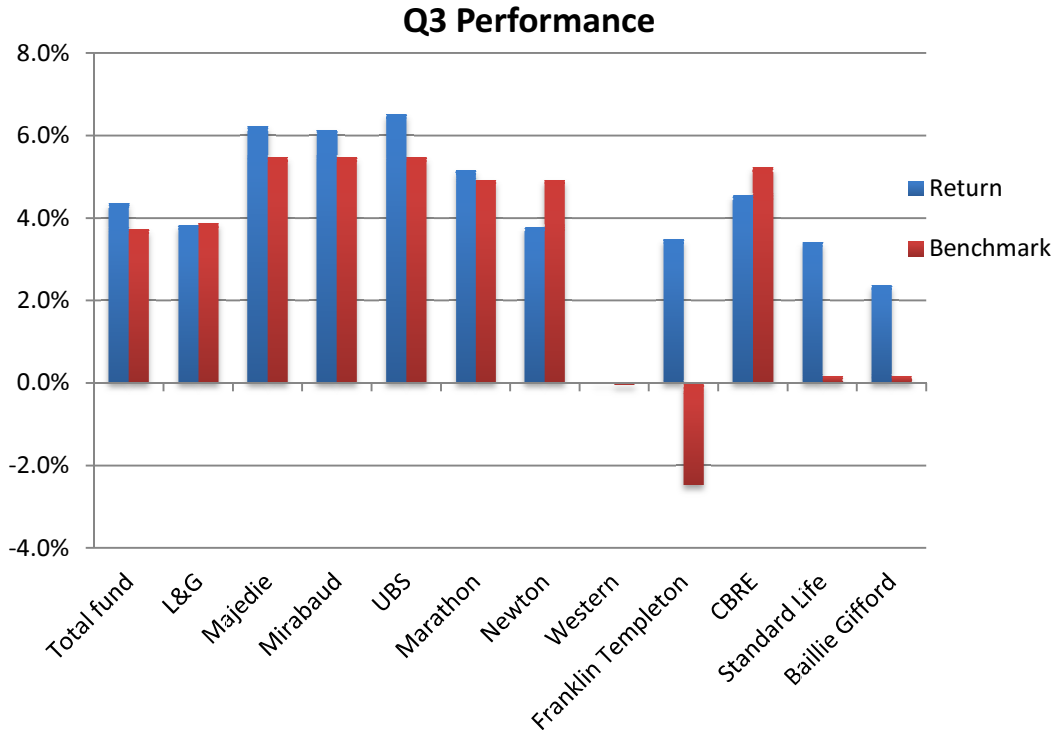




## 2. Fund Performance

### Summary of Quarterly Results

Overall, the total fund returned +4.4% in Q3 2013/14 above the SCC customised benchmark of 3.71%



*Both Baillie Gifford and Standard Life are absolute return funds with a benchmark based upon short term cash holdings.*

The below table shows manager performance for Q3 against manager specific benchmarks using custodian data.

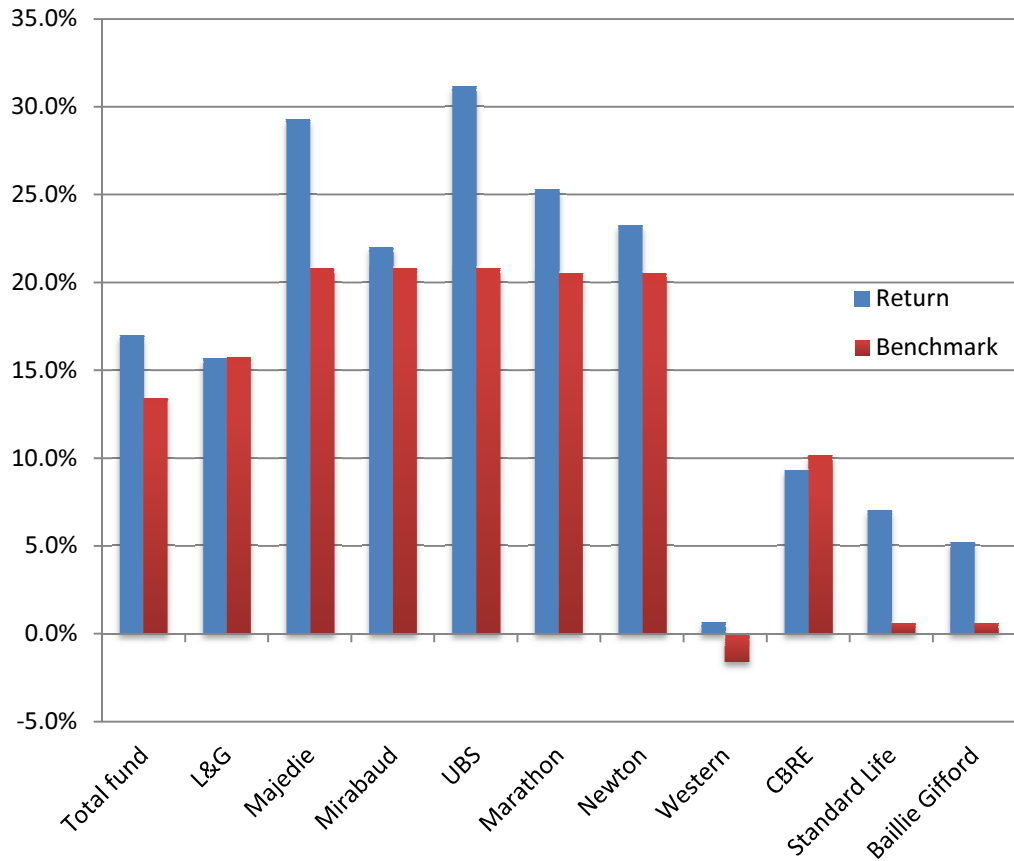
<b>Manager</b>	<b>Performance %</b>	<b>Benchmark %</b>
Total Fund	4.4	3.7
L&G	3.8	3.9
Majedie	6.2	5.5
Mirabaud	6.1	5.5
UBS	6.5	5.5
Marathon	5.2	4.9
Newton	3.8	4.9
Western	0.0	-0.1
Franklin Templeton	3.5	-2.5
CBRE	4.6	5.2
Standard Life	3.4	0.2
Baillie Gifford	2.4	0.2

*Franklin Templeton is measured against a US Dollar denominated benchmark which is then converted back to Sterling. This is the cause of the significant disparity between performance and benchmark. The benchmark is +2.2% in US Dollar terms leaving a still impressive outperformance of +1.3%.*

## Summary of Full Year Results

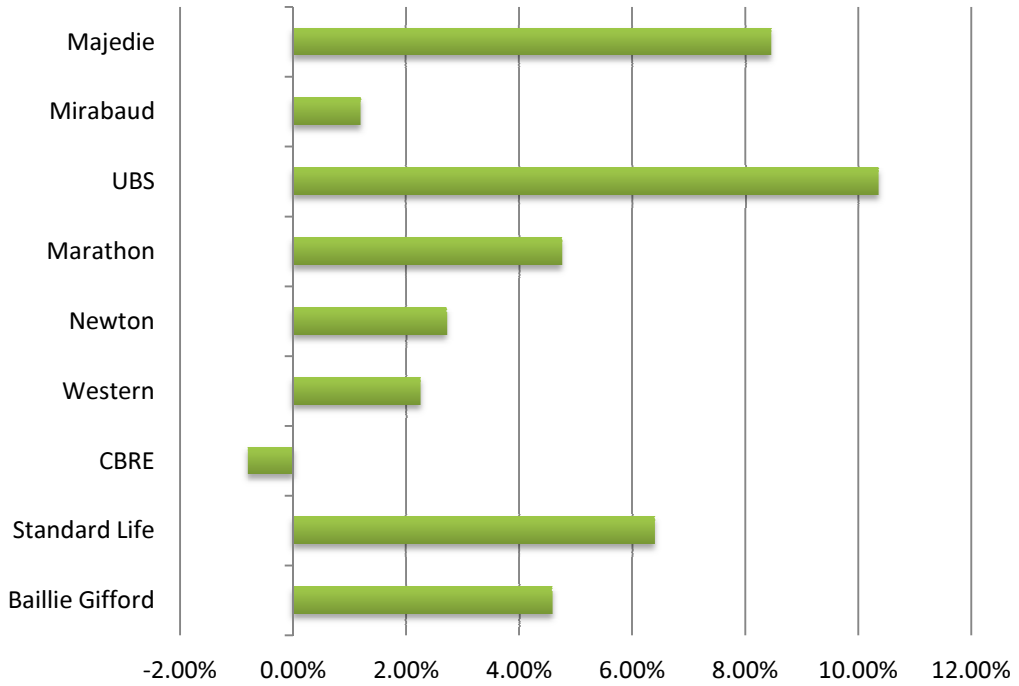
Over the past 12 months to 31 September 2013, the Fund returned 17.0% overall, surpassing the benchmark return of 13.4%.

### Rolling Full Year Performance



Equities again provided substantial investment returns over the period with significant above benchmark returns from active UK equity managers UBS and Majedie. Overseas equity through both passive and active management produced strong returns during the previous year.

### Full Year Relative Performance to Benchmark

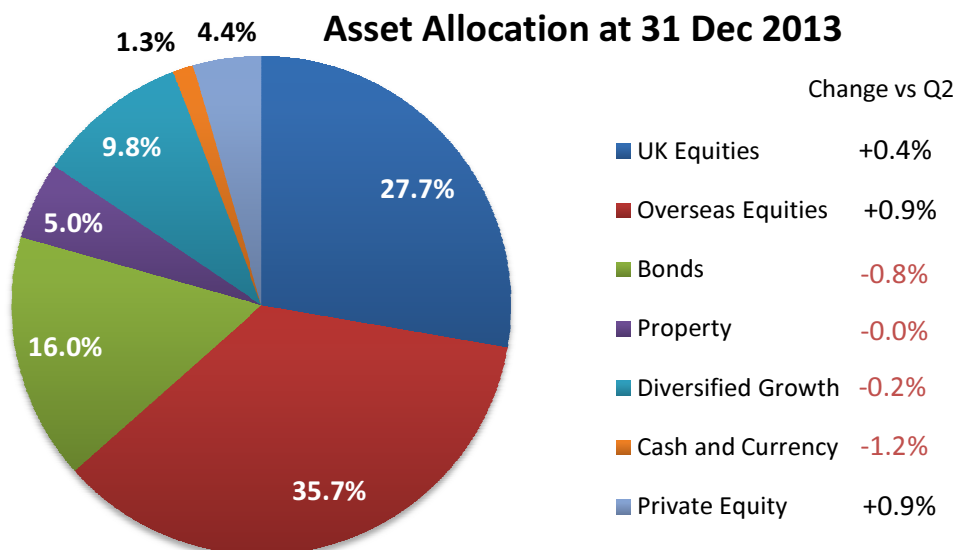


The below table shows manager performance for the year to 31 December 2013 against manager specific benchmarks using custodian data.

Manager	Performance %	Benchmark %
Total Fund	17.0	13.4
L&G	15.7	15.7
Majedie	29.3	20.8
Mirabaud	22.0	20.8
UBS	31.2	20.8
Marathon	25.3	20.5
Newton	23.2	20.5
Western	0.6	-1.6
CBRE	9.3	10.1
Standard Life	7.0	0.6
Baillie Gifford	5.2	0.6

### 3. Asset Allocation

The graph and table below summarise the asset allocation of the managed elements of the fund, excluding private equity holdings and internally held cash balances.

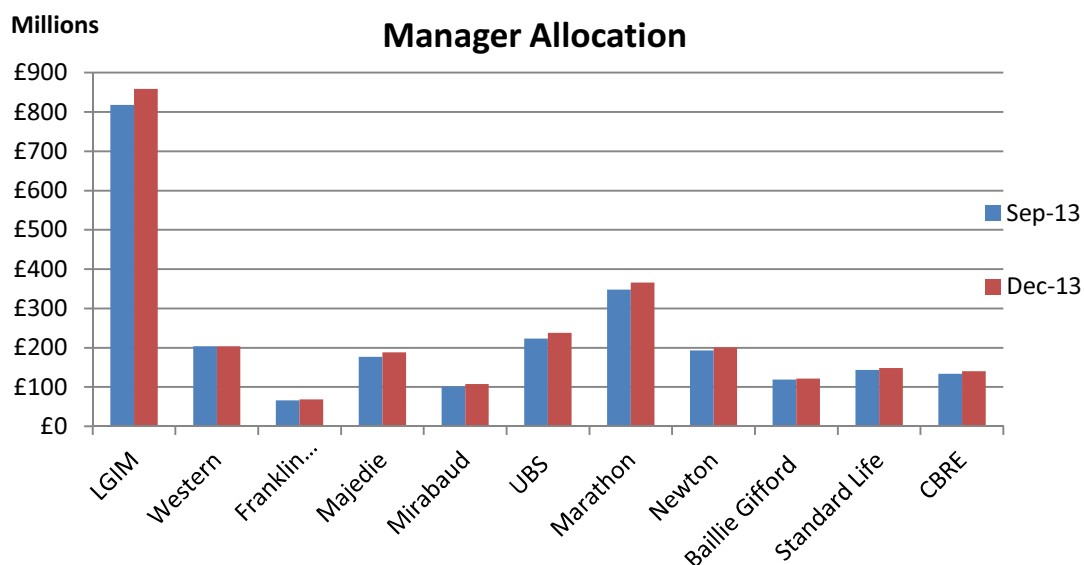


The table below compares the actual asset allocation as at 31 December 2013 against target asset weightings.

	TOTAL FUND	Actual	Target	Last Quarter	
				£m	%
	£m	%	%	£m	%
<b>Fixed Interest</b>					
UK Government	121.0	4.4	5.0	119.1	4.4
UK Non-Government	159.5	5.8	7.6	159.5	6.1
Overseas	0.0	0.0	0.0	0.0	0.0
Total Return	68.8	2.5	2.7	66.4	2.5
<b>Index Linked</b>	89.9	3.3	3.8	96.4	3.7
<b>Equities</b>					
UK	761.8	27.7	27.5	719.2	27.4
Overseas	982.2	35.7	32.3	915.1	34.8
<b>Property Unit Trusts</b>	138.5	5.0	6.6	132.8	5.1
<b>Diversified growth</b>	269.7	9.8	9.5	262.0	10.0
<b>Cash</b>	24.0	0.9	0.0	49.3	1.9
<b>Currency hedge</b>	12.7	0.5	0.0	18.2	0.6
<b>Private Equity</b>	121.4	4.4	5.0	91.1	3.5
<b>TOTAL</b>	<b>2,749.5</b>	<b>100.0</b>	<b>100.0</b>	<b>2,629.1</b>	<b>100.0</b>

#### 4. Manager Allocation

The graph below shows the current manager allocation.



The table below includes the actual and target manager allocation weightings for those investments managed through the custodian Northern Trust as at 31 December 2013. This excludes the internal cash and private equity portfolio.

Investment Manager	Asset Class	Market Value £m	Actual Allocation %	Target Allocation %
LGIM	Multi-Asset	858.9	32.5	33.0
Western	Bonds	204.2	7.7	8.25
Franklin Templeton	Bonds	68.8	2.6	2.75
Majedie	UK Equity	188.4	7.1	7.0
Mirabaud	UK Equity	107.9	4.1	4.0
UBS	UK Equity	238.0	9.0	8.0
Marathon	Global Equity	366.3	13.9	12.0
Newton	Global Equity	200.8	7.6	8.0
Baillie Gifford	Diversified Growth	121.6	4.6	4.0
Standard Life	Diversified Growth	148.1	5.6	6.0
CBRE	Property	140.3	5.3	7.0
	Residual Cash	0.9	0.0	0.0
<b>TOTAL</b>		<b>2,644.2</b>	<b>100.0</b>	<b>100.0</b>

## **CONSULTATION:**

6 The Chairman of the Pension Fund Board has been consulted on this report.

## **RISK MANAGEMENT AND IMPLICATIONS:**

7 Risk related issues have been discussed and are contained within the report.

## **FINANCIAL AND VALUE FOR MONEY IMPLICATIONS**

8 Financial and value for money implications are discussed within the report.

## **CHIEF FINANCE OFFICER COMMENTARY**

9 The Chief Finance Officer is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

## **LEGAL IMPLICATIONS – MONITORING OFFICER**

10 There are no legal implications or legislative requirements associated with this report.

## **EQUALITIES AND DIVERSITY**

11 The approval of the various options will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

## **OTHER IMPLICATIONS**

12 There are no potential implications for council priorities and policy areas.

## **WHAT HAPPENS NEXT**

13 The following next steps are planned:

- Implementation of the various recommendation approvals.

---

### **Contact Officer:**

Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

### **Consulted:**

Pension Fund Board Chairman

### **Annexes:**

1. Asset Allocation Policy and Actual as at 31 December 2013 and 31 January 2014
2. Hymans Robertson briefing on ill health insurance
3. Notes from fund manager meetings 4 February 2014

### **Sources/background papers:**

None

---

This page is intentionally left blank