



**AUDIT & GOVERNANCE COMMITTEE**  
**6 December 2012**

**PENSION FUND INVESTMENTS – SEPTEMBER QUARTER 2012**

**SUMMARY AND PURPOSE:**

This report deals with the investment transactions of the pension fund during the September quarter and the position of the fund as at 30 September 2012, together with other matters considered by the Investment Advisors Group (IAG) at its quarterly meeting of 16 November 2012.

**RECOMMENDATION:**

It is recommended that the committee note the content of the pension fund report for the quarter to 30 September 2012.

**BACKGROUND:**

1. The Investment Advisors Group is responsible for monitoring the activities of the Surrey Pension Fund and reporting to the county council and other employing bodies. This is achieved through the presentation of a quarterly report to the Audit and Governance Committee.

**PENSION FUND INVESTMENTS – SEPTEMBER QUARTER 2012:**

**Position Statement as at 30 September 2012**

2. The market value of the fund increased during the quarter from £2,151.5 million at 30 June 2012 to £2,236.9 million at 30 September 2012, an increase of 3.9%. The value of the fund as at close of business on 9 November is estimated at £2,259.0 million.
3. The value of the major asset classes at 30 September 2012 compared with 30 June 2012 was as follows:

	30 September		30 June	
	£m	%	£m	%
<b>Fixed Interest</b>				
UK Government	109.3	4.9	127.2	5.9
UK Non-Government	180.1	8.1	174.7	8.1
Overseas	44.5	2.0	17.0	0.8
<b>Index Linked</b>	83.3	3.7	86.6	4.0
<b>Equities</b>				
UK	633.1	28.3	633.0	29.4
Overseas	749.0	33.5	704.0	32.7
<b>Property Unit Trusts</b>	121.3	5.4	120.3	5.6
<b>Private Equity</b>	84.5	3.8	90.3	4.2
<b>Diversified Growth</b>	157.7	7.0	153.5	7.1
<b>Cash</b>	67.3	3.0	51.4	2.4
<b>Currency hedge*</b>	6.8	0.3	-6.5	-0.3
<b>Total Fund</b>	<b>2,236.9</b>	<b>100.0</b>	<b>2,151.5</b>	<b>100.0</b>

\* Net unrealised profit/loss

4. The following table shows the breakdown of the market valuation as at 30 September 2012 by asset class and compares the totals with the target asset allocation. The total excludes any private equity funds or cash held by SCC included in the table above.

	TOTAL FUND £m	Actual %	Target %	Last Quarter	
				£m	%
<b>Fixed Interest</b>					
UK Government	109.3	5.1	8.0	127.2	6.2
UK Non-Government	180.1	8.5	8.0	174.7	8.5
Overseas	44.5	2.1	0.0	17.0	0.8
<b>Index Linked</b>	83.3	3.9	4.0	86.6	4.2
<b>Equities</b>					
UK	633.1	29.7	28.0	633.0	30.8
Overseas	749.0	35.2	35.0	704.0	34.3
<b>Property Unit Trusts</b>	121.3	5.7	7.0	120.3	5.9
<b>Diversified growth</b>	157.7	7.4	10.0	153.5	7.5
<b>Cash</b>	45.1	2.1	0.0	43.4	2.1
<b>Currency hedge</b>	6.8	0.3	0.0	-6.5	-0.3
<b>TOTAL</b>	<b>2,130.2</b>	<b>100.0</b>	<b>100.0</b>	<b>2,053.2</b>	<b>100.0</b>

5. The following table breaks down the above to show the value of assets held by individual managers at quarter end:

	£m	Actual %	TARGET	LAST QUARTER	
			%	£m	%
<b>Multi-Asset</b>					
LGIM	743.1	34.9	32.0	722.2	35.2
<b>Bonds/Property</b>					
Western	266.6	12.5	11.0	255.7	12.5
CBRE	127.1	6.0	7.0	126.7	6.2
<b>UK Equity</b>					
Majedie	136.2	6.4	8.0	128.6	6.3
Mirabaud	85.9	4.0	4.0	83.6	4.1
UBS	170.0	8.0	8.0	160.9	7.8
<b>Global Equity</b>					
Marathon	280.7	13.2	12.0	269.3	13.1
Newton	161.9	7.6	8.0	152.6	7.4
<b>Diversified Growth</b>					
Baillie Gifford	31.1	1.5	4.0	30.4	1.5
Standard Life	126.6	5.9	6.0	123.1	6.0
<b>Residual Cash</b>	1.0	0.0	0.0	0.0	0.0
<b>TOTAL</b>	<b>2,130.2</b>	<b>100.0</b>	<b>100.0</b>	<b>2,053.2</b>	<b>100.0</b>

6. In July 2011 the Investment Advisors Group (IAG) started to review the investment strategy of the fund following the implementation of the 2010 actuarial valuation results. Changes to the investment strategy were approved by the IAG in March 2012 and began to be implemented in the June quarter.
7. During the June quarter, the regional specialist equity managers, JP Morgan & TCW, had their mandates terminated. The proportion of the fund managed by UBS was reduced from 13% to 8%. Index-linked bonds valued at around £60m were transferred from Western to Legal & General to be managed on a passive basis. The fund also made investments in diversified growth funds managed by Standard Life and Baillie Gifford. The diversified growth portfolio became fully funded on 8 November 2012 with the final transfer to Baillie Gifford to bring their total funding up to £75m.
8. As part of the review the IAG also agreed to invest an additional £30m in global equities managed by Majedie. During the September quarter, Majedie announced that key staff from its global team would be leaving the firm and joining Marathon. The additional funding for Majedie has been suspended, pending further consideration.

9. At the IAG meeting it was agreed that Mirabaud, currently mandated to invest in UK Equities, will be able to invest up to 20% in Global Equities. The benchmark will remain as the FTSE100. This is the same agreement that Majedie has in place for its UK equity mandate.
10. The IAG also discussed the possibility of changing the bond mandate with Western. The current bond benchmark is split: 50% gilts and 50% non-gilts. The Group feels now is the right time to decrease the allocation to gilts and move to a total return or absolute return strategy, involving global credit, emerging market debt and high yield bonds.
11. It was agreed that 50% of the current allocation to gilts could be used to fund this. Officers were asked to speak to the fixed income fund manager about the proposals and the final decision would be delegated to the Section 151 Officer and the Chairman of the IAG.
12. In the September quarter contributions from members exceeded the value of benefits paid and transfer values by £6.1m. Investment income (net of costs) totaled £8.9m. Market movements increased the value of the fund by £70.3m.

### Investment Performance Results for the Period

13. The managed fund made a return of 4.2% over the quarter. This compares with a total fund customised benchmark return of 3.6%. The total fund return for the year to the end of September was 15.1% above the benchmark return of 14.4%.
14. For the quarter to 30 September performance returns for the individual fund managers, in absolute terms and relative to their benchmark target, were as follows:

Manager	Asset Class	Market Value 30 June	Market Value 30 September	Return %	Relative %
<b>Multi-Asset</b>					
LGIM	Multi-Asset	722.2	743.1	3.4	0.1
<b>Bonds/Property</b>					
Western	Bonds	255.7	266.6	4.3	0.9
CBRE	Property	126.7	127.1	0.8	0.4
<b>Equity</b>					
Majedie	UK	128.6	136.2	6.2	1.5
Mirabaud	UK	83.6	85.9	3.0	-1.7
UBS	UK	160.9	170.0	5.8	1.1
Marathon	Global	269.3	280.7	4.3	0.6
Newton	Global	152.6	161.9	6.2	2.4
<b>Diversified Growth</b>					
Standard Life	Diversified Growth	123.1	126.6	2.8	2.6
Baillie Gifford	Diversified Growth	30.4	31.1	2.1	2.0
<b>TOTAL MANAGED FUND</b>		<b>2,053.2</b>	<b>2,130.2</b>	<b>4.2</b>	<b>0.8</b>

15. In summary in the quarter to 30 September 2012:
- The total fund return of 4.2% was greater than the customised (hedged) benchmark return of 3.6% (+0.6%).
  - In absolute terms, the best performing managers were Newton and Majedie with a return of 6.2%. This compared to a benchmark return of 3.8% (+2.4%) for Newton and 4.7% (+1.5%) for Majedie.
  - Excluding the diversified growth fund managers, in relative terms, the best performing manager was Newton (+2.4%). The diversified growth fund managers are excluded because these investments are benchmarked against cash returns which are generally low. These managers have significant out performance targets which means that the relative performance of these investments should be high.
  - All managers outperformed relative to benchmark except for Mirabaud (-1.7%). Mirabaud state that their performance was held back by their limited exposure to financial stocks which performed well in the period following the announcement of additional quantitative easing.
16. Under the fund's current strategy, short-term periods of underperformance (e.g. over individual quarters or years) should be expected. The overriding objective of the portfolio is to outperform the customised benchmark by 1% per annum over a rolling three-year period.
17. Each manager has a different target, depending on the type of mandate that they have. Having managers with different targets and different but complimentary styles means that short-term periods of underperformance are likely, with the expectation for the manager to perform over the longer-term.
18. In the year to 30 September 2012 and in the period since inception (2004 for all managers, apart from Newton (December 2007) and Standard Life and Baillie Gifford (May 2012), performances for the individual managers were as follows:

Manager	Return for Year	Relative Performance to 30 Sep			Target Outperformance*
		%	year	3 years	
		p.a.	p.a.	p.a.	
<b>Multi-Asset</b>					
LGIM	13.1	0.0	0.0	0.1	n/a
<b>Bonds/Property</b>					
Western	12.9	1.2	-0.9	-1.0	0.75
CBRE	1.2	-1.9	-1.0	-1.7	1.0
<b>Equity</b>					
Majedie	15.6	-1.6	0.5	3.5	2.5
Mirabaud	17.4	0.1	-0.1	1.9	2.5
UBS	18.8	1.5	-1.4	-1.2	2.0
Marathon	18.5	4.2	4.8	3.5	2.0
Newton	19.0	2.3	-0.3	-0.9	2.0
<b>Diversified Growth</b>					
Standard Life	n/a	n/a	n/a	0.8	5.0
Baillie Gifford	n/a	n/a	n/a	2.2	3.5
<b>TOTAL MANAGED FUND</b>	<b>15.1</b>	<b>0.7</b>	<b>-0.1</b>	<b>-0.2</b>	<b>1.5</b>

\*Standard Life outperformance target is gross of fees, all others net.

19. Over a rolling 3-year period:
- Marathon (+4.8%) achieved a return ahead of their performance target.
  - Majedie (+0.5%) outperformed compared to benchmark.
  - UBS (-1.4%), Western (-0.9%), and CBRE (-1.0%) all underperformed compared with benchmark.
20. The overriding objective of the portfolio is to outperform the customised benchmark by 1% per annum over a rolling three-year period. Managers that underperform compared to benchmark over that period hamper the fund achieving its objective. The IAG continually monitors the performance of all managers and also monitors current developments to assess whether each manager has the ability to meet its target and help the fund achieve its objective.
21. The fund's performance is also measured with reference to a Local Authority average return (as calculated by the WM Company). These figures are not yet available but will be provided at the meeting.

#### **Quarterly IAG Meeting 16 November 2012**

22. The IAG received a briefing on the market value and performance of the Fund as covered in Paragraphs 13-21 of this report.

## **IMPLICATIONS:**

Financial:

There are no direct financial implications.

Equalities:

There are no direct equality implications.

Risk management and value for money:

Pension Fund risks are proactively monitored by officers and the Fund's Investment Advisors Group.

## **WHAT HAPPENS NEXT:**

The next meeting of the IAG will take place in February 2013.

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### **REPORT AUTHOR:**

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### **CONTACT DETAILS:**

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

Investment Advisors Group meeting papers

Reports sourced from SAP, the Fund custodian, Fund Managers and WM Company

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