

SURREY COUNTY COUNCIL**SURREY PENSION FUND COMMITTEE****DATE: 18 SEPTEMBER 2015****LEAD OFFICER: SHEILA LITTLE, DIRECTOR OF FINANCE****SUBJECT: MANAGER ISSUES AND INVESTMENT PERFORMANCE****SUMMARY OF ISSUE:**

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

RECOMMENDATIONS:

It is recommended that the Surrey Pension Fund Committee:

1. Note the report.
2. Give consideration to infrastructure as a future strategy for the Fund.

REASON FOR RECOMMENDATIONS:

In order to achieve best possible performance alongside optimal risk.

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

Manager	Issue	Status/Action Required
L&G	Possible Rebalancing	The asset allocation is within the Fund's policy control limits. The asset allocations at 30 June 2015 and 31 August 2015 are shown in Annex 1.
Western	Multi Asset Credit	At its meeting on 23 July 2015, the Committee approved the appointment of Western Asset Management to run a multi asset credit portfolio. The transition process is expected to be completed by the end of October 2015. A transition report will be presented to the Committee at its 13 November 2015 meeting.
Western, Newton, CBRE, Standard Life	Client meeting	Update of minutes of external fund manager meetings held on 7 September 2015 shown in Annex 2.

2) Freedom of Information Requests

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

Date of Response	Organisation	Request	Response
03 June 2015	Pitchbook	Private equity investment information	Investment summary taken to previous meeting of Pension Fund Committee
30 June 2015	Inframation Group	Private equity investment information	Investment summary taken to previous meeting of Pension Fund Committee

3) **Future Pension Fund Committee Meetings/Pension Fund AGM**

The schedule of meetings for 2015 and 2016 is as follows:

- 18 September 2015: Committee meeting hosted at County Hall.
- 13 November 2015: Committee meeting hosted at County Hall.
- 20 November 2015: AGM hosted at County Hall
- 12 February 2016: Committee meeting hosted at County Hall.
- 13 May 2016: Committee meeting hosted at County Hall.
- 9 September 2016: Committee meeting hosted at County Hall.
- 11 November 2016: Committee meeting hosted at County Hall.
- 18 November 2016: AGM hosted at County Hall

4) **Local Pension Board**

The Local Pension Board met for the first time on 27 July 2015. A separate report on the Local Pension Board is included in the agenda.

5) **Stock Lending**

In the quarter to 30 June 2015, stock lending earned a net income for the Fund of £135k with an average value on loan equal to £162.5m.

6) **Private Equity**

A separate report is included in the agenda.

7) **Internally Managed Cash**

The internally managed cash balance of the Pension Fund was £14m as at 30 June 2015. As at 8 September 2015, the cash balance was £32m.

8) **Liability Driven Investment (LDI) Framework**

At its meeting on 13 February 2015, the Committee agreed to set the real yield trigger for future LDI leverage to 0.27% and this was incorporated into the mandate documentation with Legal & General (LGIM).

Now that the implementation for the leveraged gilt mandate has been completed, the Committee will regularly monitor movements in real yields and, specifically, the trigger that has been agreed.

Mercer has produced a simple one page document for this, shown as Annex 3. This will be shown produced at every future Committee meeting.

There will be element of ongoing training with this annex, with a regular reminder of the relationship between changes in yields (including the volatility in how these can move up and down) and the impact this has on the value placed on the liabilities.

9) Infrastructure

Included within the agenda is a training session on infrastructure from an investment strategy perspective: the case for infrastructure, expected benefits, potential risks and how to implement. Papers on this training session will be sent out prior to the meeting. The training will be provided from 9:30am to 11:00am before the meeting commences at 11:00am.

It is suggested that members give consideration to the asset class as a strategy for the Fund.

10) Multi Asset Credit

At its meeting on 23 July 2015, the Pension Fund Board appointed Western Asset Management to run a Multi Asset Credit portfolio with funds from the LGIM investment grade bonds and the Western UK gilts. The due diligence process is currently under way with the transition of funds expected to be completed by the end of October 2015. A transition report will be provided to the 13 November 2015 committee meeting.

11) Employer Body Admission/Termination Guidance

At its meeting on 22 May 2015, the Surrey Pension Fund Committee agreed to the Fund establishing new guidance for scheme employers, which reflects a more structured and focused approach to risk assessment.

Officers have had further meetings with the Fund actuary to set out the scope of the project. This will include guidance to prospective new employers and established employers within the Fund.

The project develops a risk based approach to linking employer covenant strength to funding solutions.

It is planned to present the draft guidance to the Pension Fund Committee for the 13 November 2015 meeting, followed by a consultation with stakeholders and a launch in line with the 2016 actuarial valuation.

12) Members' Training

The results of member training assessments were tabled at the 13 February 2015 meeting. The six main areas of desired future training for 2015/16 as highlighted by the results are as follows:

1. Stock lending
2. Role of the global custodian
3. Currency/foreign exchange management
4. Infrastructure
5. LGPS Regulatory background
6. Admissions/Termination Policy

The Strategic Finance Manager (Pension Fund and Treasury) will arrange as appropriate. For the 18 September meeting, infrastructure will be the topic with training arranged from 9:30am onwards. The Fund's actuary will also introduce a session on the upcoming actuarial valuation and deficit management.

The Chairman has also completed one-to-one meetings with individual Committee members to discuss their training needs.

13) Pension Fund Committee Effectiveness (Self Assessment)

At the meeting of 22 May 2015, the Board agreed to self assess its effectiveness over the financial year 2014/15. The results of the process by the ten Board members are shown in Annex 4.

14) Fund Manager Meetings of 7 September 2015

Notes of the fund manager meetings of 7 September 2015 are shown in Annex 2.

Report of the Strategic Finance Manager

Financial and Performance Report

1. Funding Level

Past Service Position	30 June 2015 £m
Past Service Liabilities	4,135
Market Value of Assets	3,127
Deficit	(1,008)
Funding Level	75.6%

The funding level at the latest formal valuation at 31 March 2013 was 72.3%. As at 30 June 2015 the funding level stood at 75.6%, an increase on the latest formal valuation and an increase versus the last quarter's funding level of 74.4%.

The following tables show the movement in the Fund's deficit. The discount rate applied at 30 June 2015 was 4.2% less than the 4.6% used for the full valuation at 31 March 2013. Unfortunately, the strong investment returns seen over the last two years are more than offset by the change in actuarial assumptions over the same period.

Valuation Period to date Reconciliation	£m
Deficit at 31 March 2013	-980
Interest on deficit	-115
Excess return on assets	222
Change in actuarial assumptions	-232
Contributions less benefits accruing	97
Deficit at 30 June 2015	-1,008

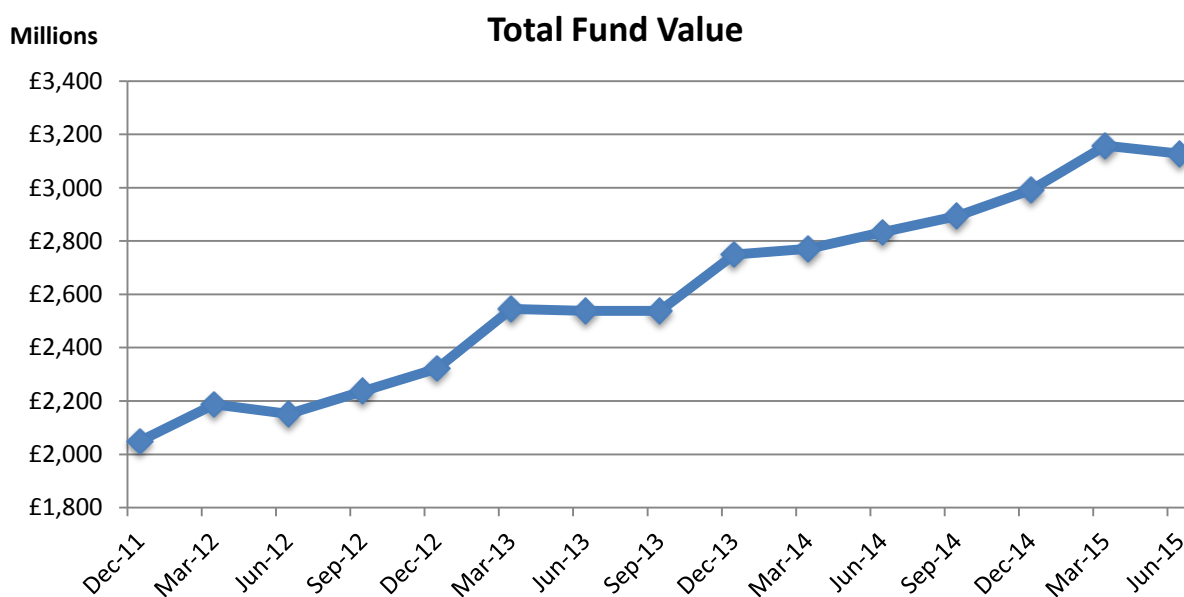
Quarterly Reconciliation	£m
Deficit at 31 March 2015	-1,087
Interest on deficit	-14
Excess return on assets	-71
Change in actuarial assumptions	150
Contributions less benefits accruing	14
Deficit at 30 June 2015	-1,008

2. Market Value

The value of the Fund was £3,127.2m at 30 June 2015 compared with £3,157.5m at 31 March 2015. The investment performance for the period was -1.7%.

The change in market value is attributed as follows:

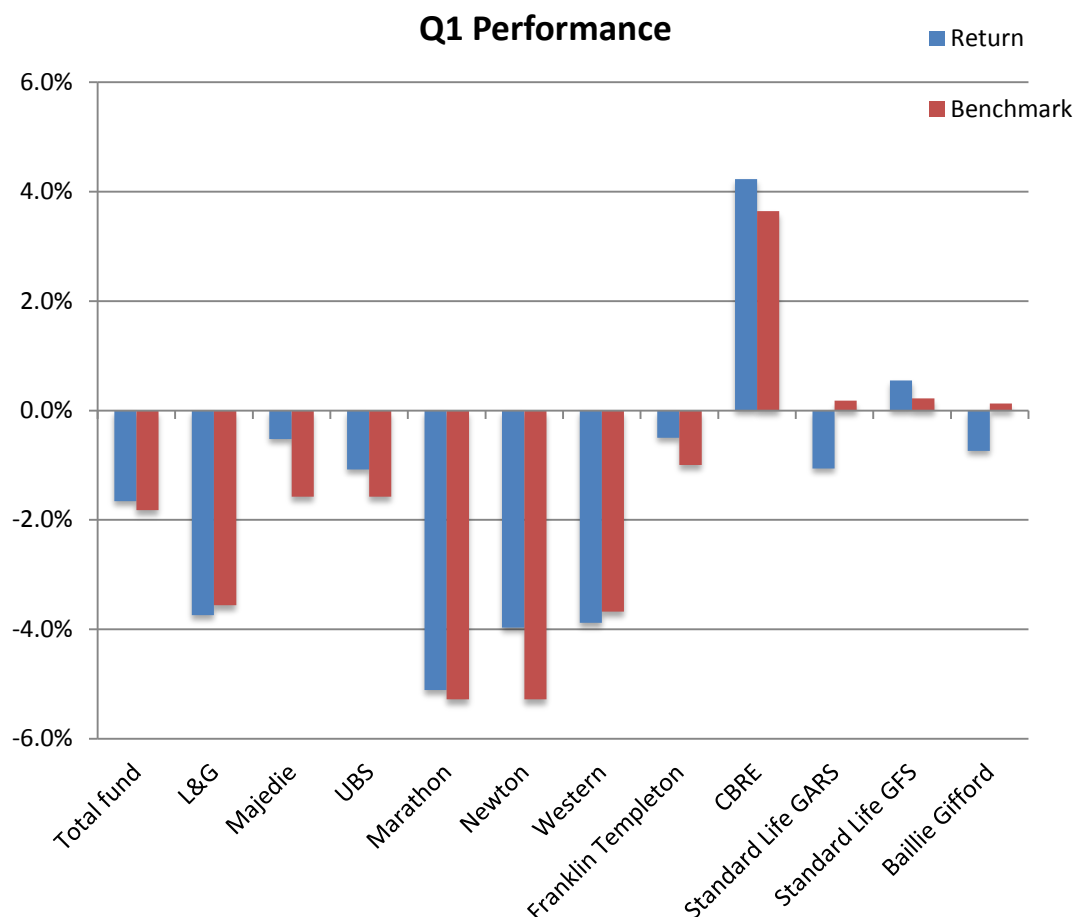
	£m
Market Value at 31/03/2015	3,157.5
Contributions less benefits and net transfer values	21.0
Investment income received	16.9
Investment expenses incurred	-2.7
Market movements	-65.4
Market Value at 30/06/2015	3,127.3
Market Value at 31/08/2015	3,060.1



3. Fund Performance

Summary of Quarterly Results (gross of investment fees)

Overall, the Fund returned -1.7% in Q1 2015/16, in comparison with the Fund's customised benchmark of -1.8%.



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

Q1 2015/16 was the first quarter of negative investment performance since the equivalent period during 2013/14. Global equities suffered from a volatile and ultimately disappointing quarter with fears over the outcome of Greek debt bailout discussions and a surprise contraction in US GDP numbers. The global equity benchmark was -5.3% for the quarter, although all active equity managers outperformed in the falling market.

Property was the only major asset class to escape unscathed with positive returns during the first quarter boosted by greater than expected GDP figures and an outright winner in the UK general election.

The table below shows manager performance for 2015/16 Q2 (gross of investment manager fees) against manager specific benchmarks using Northern Trust data.

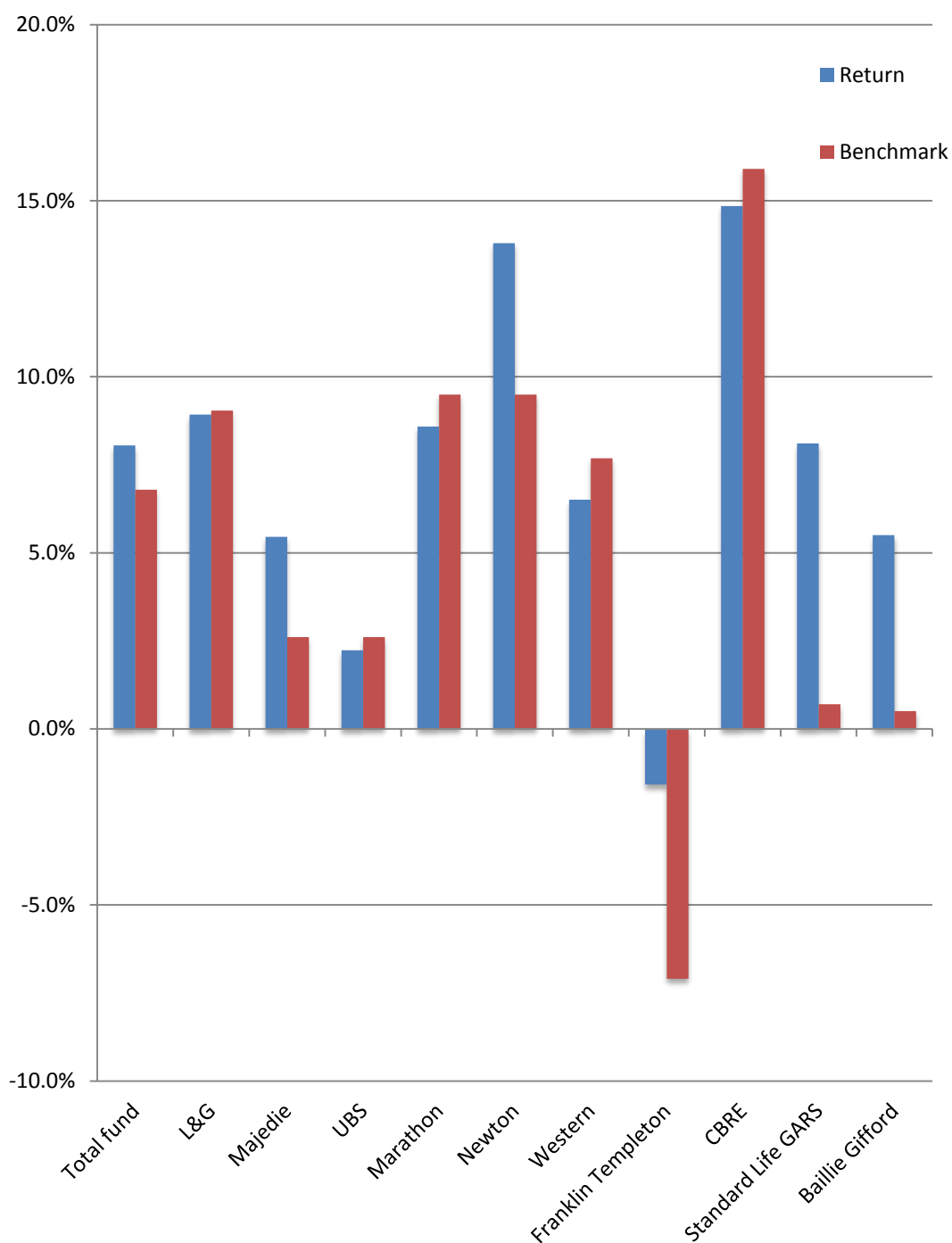
Manager	Performance %	Benchmark %	Relative %
Total fund	-1.7	-1.8	0.1
L&G	-3.7	-3.6	-0.1
Majedie	-0.5	-1.6	1.1
UBS	-1.1	-1.6	0.5
Marathon	-5.1	-5.3	0.2
Newton	-4.0	-5.3	1.3
Western	-3.9	-3.7	-0.2
Franklin Templeton	-0.5	-1.0	0.5
CBRE	4.2	3.6	0.6
Standard Life GARS	-1.1	0.2	-1.3
Standard Life GFS	0.5	0.2	0.3
Baillie Gifford	-0.7	0.1	-0.8

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

Summary of Full Year Results (gross of investment fees)

During the course of the previous 12 months to 30 June 2015, the Fund returned +8.0% overall against the customised benchmark of +6.8%.

Rolling Full Year Performance



Consistent, strong returns from property led to CBRE reporting the largest absolute return over the past 12 months with +14.8% but below the benchmark return of +15.9%.

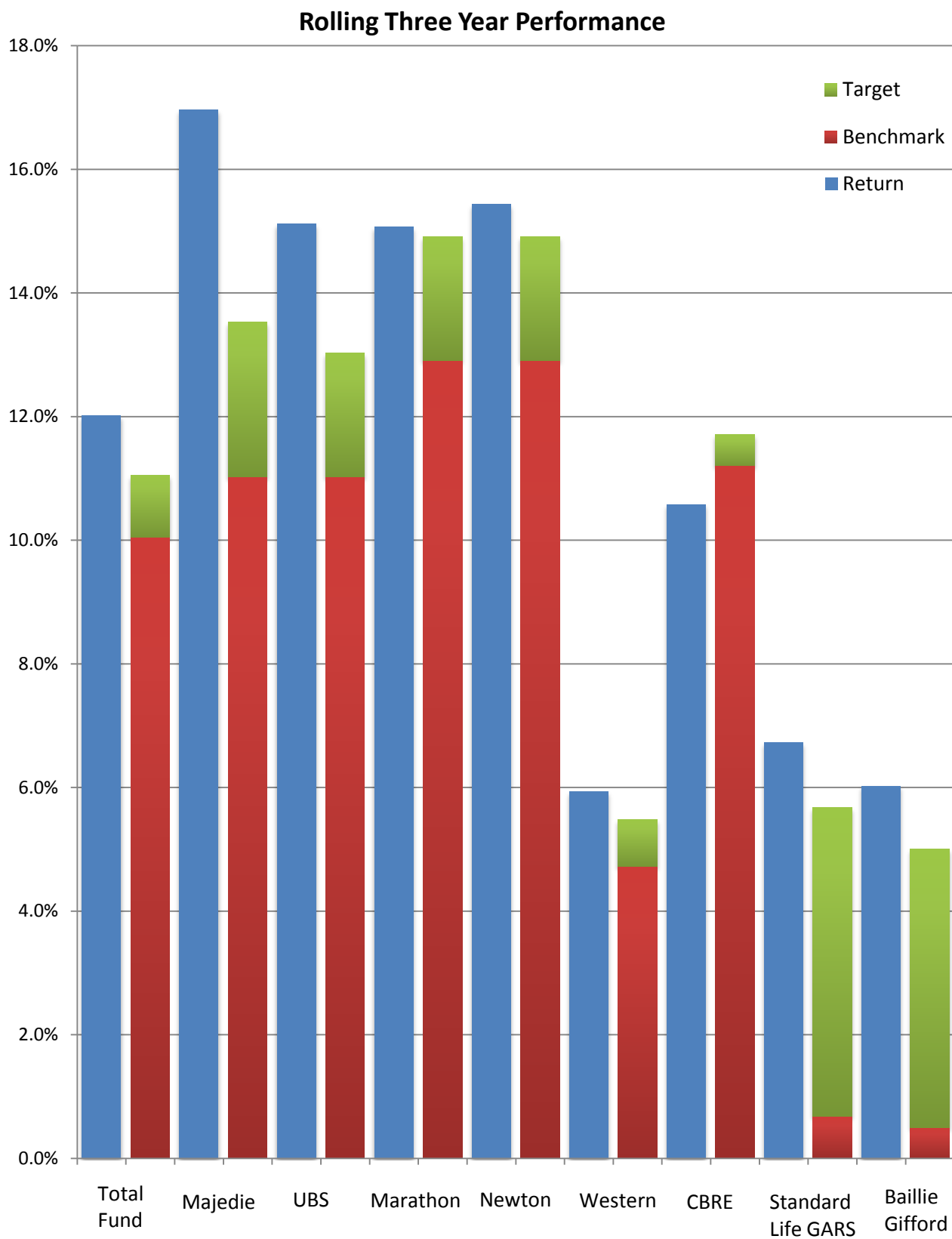
Global equities were a key driver of returns during the year with Newton in particular reporting +13.8% and outperformance of +4.3% against the wider index.

The table below shows manager performance for the year to 30 June 2015 against manager specific benchmarks using custodian data.

Manager	Gross of Fees Performance %	Benchmark %	Relative %	Net of Fees Performance %
Total fund	8.0	6.8	1.2	7.7
L&G	8.9	9.0	-0.1	8.8
Majedie	5.5	2.6	2.9	4.5
UBS	2.2	2.6	-0.4	1.6
Marathon	8.6	9.5	-0.9	8.0
Newton	13.8	9.5	4.3	13.6
Western	6.5	7.7	-1.2	6.3
Franklin Templeton	-1.6	-7.1	5.5	-2.2
CBRE	14.8	15.9	-1.1	14.1
Standard Life GARS	8.1	0.7	7.4	7.5
Baillie Gifford	5.5	0.5	5.0	4.9

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

Summary of Rolling Three Year Performance

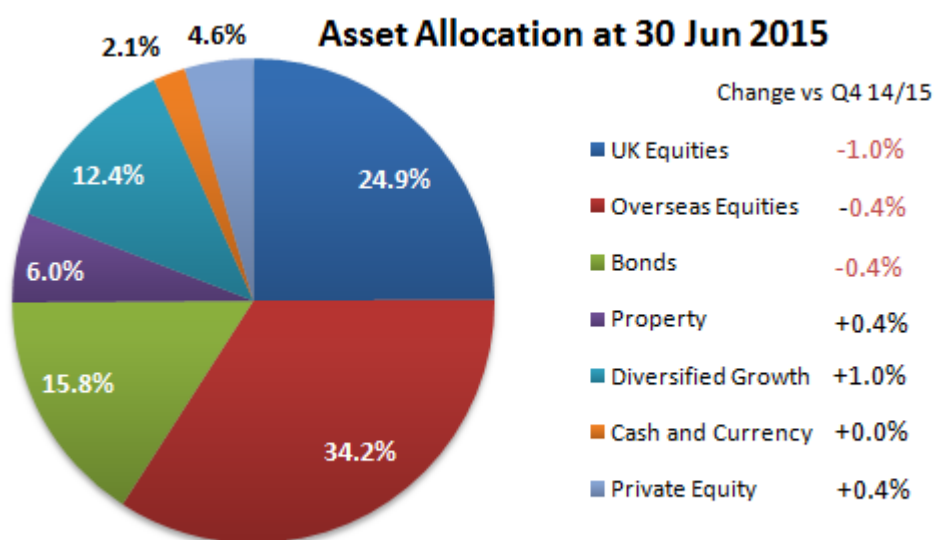


The below table shows the annualised performance by manager for the previous three years.

Manager	Performance %	Benchmark %	Target %	Relative %
Total fund	12.0	10.1	11.1	0.9
Majedie	17.0	11.0	13.5	3.5
UBS	15.1	11.0	13.0	2.1
Marathon	15.1	12.9	14.9	0.2
Newton	15.4	12.9	14.9	0.5
Western	5.9	4.7	5.5	0.4
CBRE	10.6	11.2	11.7	-1.1
Standard Life GARS	6.7	0.7	5.7	1.0
Baillie Gifford	6.0	0.5	5.0	1.0

4. Asset Allocation

The graph and table below summarise the asset allocation of the fund as at the 30 June 2015.

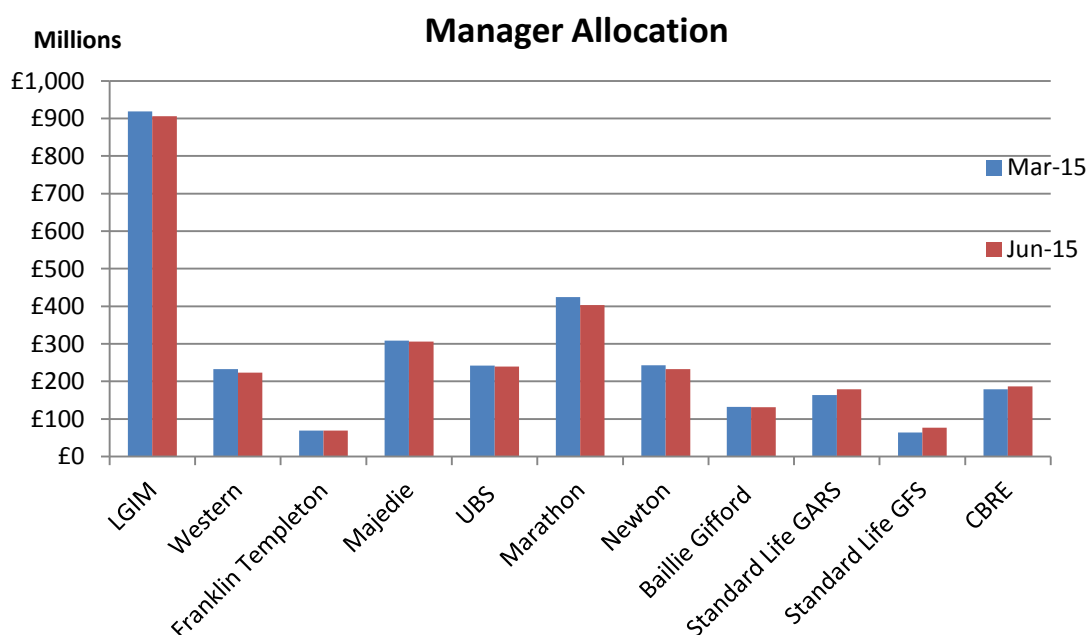


The table below compares the actual asset allocation as at 30 June 2015 against target asset weightings.

	TOTAL FUND	Actual	Target	Last Quarter	
	£m	%	%	£m	%
Fixed Interest					
UK Government	62.8	2.0	2.6	66.8	2.1
UK Non-Government	130.9	4.2	7.1	133.5	4.2
Overseas	75.0	2.4	0.0	80.8	2.6
Total Return	69.0	2.2	2.4	69.5	2.2
Index Linked	155.7	5.0	5.5	161.3	5.1
Equities					
UK	779.7	24.9	27.5	816.7	25.9
Overseas	1,068.6	34.2	32.3	1,091.4	34.6
Property Unit Trusts	187.4	6.0	6.2	176.1	5.6
Diversified growth	387.4	12.4	11.4	360.1	11.4
Cash	62.1	2.0	0.0	76.9	2.4
Currency hedge	5.0	0.1	0.0	-8.2	-0.3
Private Equity	143.6	4.6	5.0	132.6	4.2
TOTAL	3,127.2	100.0	100.0	3,157.5	100.0

5. Manager Allocation

The graph below shows the current manager allocation.



6. Fees

The following table shows a breakdown of fees paid during Q1 2015/16

Manager	Market Value 30/06/2015 £m	Manager Fees Q1 £000	Annualised Average Fee
L&G	906.1	165	0.07%
Western	223.5	133	0.24%
Franklin Templeton*	69.0	114	0.66%
Majedie	306.3	266	0.35%
UBS	239.6	72	0.12%
Marathon	402.8	463	0.46%
Newton	233.1	160	0.28%
Baillie Gifford*	131.4	174	0.53%
Standard Life GARS*	179.0	282	0.63%
Standard Life GFS*	77.0	174	0.91%
CBRE	187.1	101	0.22%
Manager Fees Total		2,110	0.28%
Tax withheld		265	
Other investment expenses		303	
Total Investment Expenses		2,678	

*Estimated, to exclude transaction fees

CONSULTATION:

- 7 The Chairman of the Pension Fund Committee has been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

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

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

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

DIRECTOR OF FINANCE COMMENTARY

- 10 The Director of Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

- 11 There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

- 12 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

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

WHAT HAPPENS NEXT

- 14 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 Committee Chairman

Annexes:

1. Asset Allocation Policy and Actual as at 30 June 2015 and 31 August 2015
2. Minutes from Quarterly Fund Manager Meetings held 07 September 2015
3. Monitoring statement re movements in real yields reference the LDI Strategy
4. Results of the Pension Fund Committee self assessment questionnaire.

Sources/background papers:

None