



Report of: **Corporate Director of Finance and Resources**

Meeting of:	Date	Agenda item	Ward(s)
Pensions Sub-Committee	16 September 2014	B2	

Delete as appropriate	Exempt	Non-exempt

Subject: PENSION FUND PERFORMANCE 1 APRIL to 30 JUNE 2014

1. Synopsis

- 1.1 This is a quarterly report to the Pensions Sub-Committee to allow the Council as administering authority for the Fund to review the performance of the Fund investments at regular intervals and review the investments made by Fund Managers quarterly.

2. Recommendations

- 2.1 To note the performance of the Fund from 1 April 2014 to 30 June 2014
- 2.2 To note the quarterly WM Company report on the overall performance updated market value and asset allocation of the fund as at 30 June 2014 at Annex A
- 2.3 To receive the presentation by Allenbridge EPIC Investment Advisers, our independent investment advisers, on our fund managers' quarterly performance attached as Appendix 2.
- 2.4 To receive a presentation from Franklin Templeton to consider cashflow projection and the proposal to re-invest the return of capital to a Franklin Templeton Private Real Estate Fund 2.
- 2.5 If recommendation 2.4 is agreed, then to delegate powers to the Corporate Director of Finance and Resources and the Assistant Chief Executive Governance and HR to undertake due diligence and agree terms.
- 2.6 To receive a presentation from Aviva, Lime Property Fund(Long Lease to Value Property Fund).

3. Fund Managers Performance for April to June 2014

3.1 The fund managers' latest quarter net performance figures compared to the benchmark is shown in the table below.

Fund Managers	Asset Allocation	Mandate	Latest Quarter Performance (April-June'14) Net of fees		12 Months to June'14 Performance Net of fees	
			Portfolio	Benchmark	Portfolio	Benchmark
LBI-In House	33%	UK equities	2.3%	2.2%	13.7%	13.1%
AllianzGI (RCM)	9%	Global equities	2.6%	2.7%	9.8%	9.6%
Newton	12%	Global equities	1.8%	2.7%	7.8%	9.6%
Legal & General	7%	Global equities	4.6%	4.7%	4.2%	4.7%
Standard Life	20%	Corporate bonds	2.3%	2.1%	8.2%	6.9%
Aviva (1)	4%	UK property	2.4%	1.6% 5.1%	8.3%	3.3% 17.6%
Threadneedle Investments (TPEN)	6%	UK commercial property	5.3%	4.3%	15.7%	13.6%
Hearthstone	2%	UK residential property	2.6%	2.1%	7.0	10.9

(1) 1.6% and 3.3% = original Gilts benchmark; 5.1% and 17.6% are the IPD All property index; for information

3.2 The WM Company quarterly report (enclosed as Annex A) gives a detailed analysis of our fund managers' latest quarter performance as well as the combined fund performance. The fund's June 2014 market value and asset allocation is also shown in this report. Members are asked to note this report.

3.3 The combined fund performance for the last quarter ending June 2014 is shown in the table below. The Fund's quarterly outperformance of 0.2% was attributable to stock selection

Combined Fund Performance	Latest Quarter Performance Net of fees		12 Months to June 2014 Performance Net of fees	
	Portfolio %	Benchmark %	Portfolio %	Benchmark %
LB of Islington Fund	2.9%	2.7%	11.2%	10.9%

3.4 Copies of the latest quarter fund manager reports are available to members for information if required.

3.5 The WM local authority universe is group of pension funds of similar characteristics but different sizes and deemed as a peer group for comparison. The Islington combined fund performance over the 1, 3 and 5 years period to June 2014 compared to its customised benchmark and percentile ranking are shown in the table below.

Period	1 year per annum	3 years per annum	5 years per annum
Combined LBI fund performance	11.2%	8.6%	12.1%
LBI customised benchmark	10.9%	8.6%	12.2%
Percentile ranking in the peer group	14	26	43

A summary page showing the fund's long term returns at asset class level with its rankings in the WM LA Universe peer group is attached as Appendix 1.

3.6 **AllianzGI (RCM)**

3.6.1 AllianzGI (formerly known as RCM) is the fund's global equity manager with a mandate to outperform the FTSE All World Index Benchmark by 3% per annum, gross of fees, measured over a 3-year rolling period from 8 June 2011.

3.6.2 In the June quarter the fund performed net of fees by returning 2.6% against a benchmark of 2.7%. Since inception in December 2008, portfolio has returned 12.9% against a benchmark of 14.4% net of fees. Relative return over three years is 2.1% per annum.

3.6.3 The portfolio value rose in absolute terms during the quarter. Stock selection in consumer goods, health care sectors, and oil & gas was positive to performance. However, stock selection in technology and industrials detracted from performance.

3.7 **Newton Investment Management**

3.7.1 Newton is the fund's other global equity manager with an inception date of 1 December 2008. The objective of the fund is to outperform the FTSE All World Index by 2.0% per annum over rolling 3 year periods, net of fees. The fund under-performed by returning 1.8% net of fees against a benchmark of 2.7% for the June quarter. Since inception the fund has delivered a relative underperformance of 0.34%. Relative return over three years is 1.22% per annum

3.7.2 The underperformance this quarter was mainly driven by stock selection in health care, technology and telecom sectors, whilst oil and gas stocks added positively to returns.

3.8 **In House Tracker**

3.8.1 Since 1992, the UK equities portfolio of the fund has been managed in-house by officers in the Loans and Investment section by passive tracking of the FTSE 350 Index. The mandate was amended as part of the investment strategy review to now track the FTSE All Share Index within a +/- 0.5% range per annum effective from December 2008. The fund returned 2.3% against a benchmark of 2.2% for the June quarter.

3.8.2 There was very little activity during the quarter apart from private equity and global property distributions and capital calls.

3.9 **Standard Life**

3.9.1 Standard Life has been the fund's corporate bond manager since November 2009. Their objective is to outperform the Merrill Lynch UK Non Gilt All Stock Index by 0.8% per annum over a 3 year rolling period. During the June quarter, the fund returned 2.3% against a benchmark of 2.1% and a 3 year relative return of 1.2% per annum.

3.9.2 The main driver behind the strong absolute returns achieved during the quarter was the combination of spread tightening and a decline in yields of the underlying government bond market. Relative outperformance was largely due to good stock selection and our overweight exposure to the financial sector and asset backed assets

3.9.3 The strategy remains to hold overweight positions in subordinated financial debt, collateralised bonds and an off-benchmark exposure to high yield, with a view to reducing some of the higher risk holdings.

3.10 **Aviva**

3.10.1 Aviva manages the fund's UK property portfolio. They were appointed in 2004 and the target of the mandate is to outperform their customised gilts benchmark by 1.5% (net of fees) over the long term. The portfolio is Long Lease to Value Property managed under the Lime Property Unit Trust Fund.

3.10.2 The fund for this quarter delivered a return of 2.4% against a gilt market of 1.6%. The All Property IPD benchmark returned 5.1% for this quarter. Since inception the fund has delivered an absolute return of 6.31% net of fees.

3.10.3 Quarter two saw the agreement of terms of 2 assets with a transaction price of £85m. The fund has maintained an unexpired average lease term of 21 years and increased diversification. Lime is well positioned to deliver attractive returns over the medium term.

3.10.4 The fund manager will be presenting to give an update on performance and outlook of the Lime fund.

3.11 **Threadneedle Property Pension Limited (TPEN)**

3.11.1 This is the fund's UK commercial pooled property portfolio that was fully funded on 14 July 2010 with an initial investment of £45 million. The net asset value at the end of June was £55.9million.

The agreed mandate guidelines are as listed below:

- 3.11.2
- Benchmark: AREF/IPD All Balanced Property Fund Index (Weighted Average) since 1 January 2014.
 - Target Performance: 1.0% p.a. above the benchmark (net of fees) over three year rolling periods.
 - Portfolio focus is on income generation with c. 75% of portfolio returns expected to come from income over the long term.
 - Income yield on the portfolio at investment of c.8.5% p.a.
 - Focus of portfolio is biased towards secondary property markets with high footfall rather than on prime markets such as Central London. The portfolio may therefore lag in speculative/bubble markets or when the property market is driven by capital growth in prime markets.

3.11.3 The fund returned 5.0% against its benchmark of 4.3% for the June quarter and a rental income yield of 6.6%. The cash balance has now been reduced to £73.2M after acquiring 6 properties during the quarter. The cash balance is now 5.6% of the fund and the aim is to maintain within a range of 5-7% throughout 2014. There is a strong asset diversification at portfolio level with a total of 250 properties. As a result of new letting activity and fixed rental value increases the fund's property portfolio rent roll is set to increase by £5.6million by 30 June 2016.

3.12 **Passive Hedge**

3.12.1 The fund currently hedges 50% of its overseas equities to the major currencies dollar, euro and yen. The passive hedge is being run by BNY Mellon our custodian. At the end of the June quarter, the hedged overseas equities returned 4.0% compared to the unhedged combined return of 3.0%.

3.13 **Franklin Templeton**

3.13.1 This is the fund's global property manager appointed in 2010 with an initial investment commitment of £25million. The agreed mandate guidelines are listed below:

- Benchmark: Absolute return
- Target Performance: Net of fees internal rate of return of 15%. Preferred rate of return of 10% p.a. with performance fee only applicable to returns above this point.
- Bulk of capital expected to be invested between 2 – 4 years following fund close.
- Distributions expected from years 6 – 8, with 100% of capital expected to be returned approximately by year 7.

3.13.2 There was a capital call of \$4.6m in August to bring total drawdown to \$23.6million and return of funds of \$6.4m. The projected net internal rate of return is 17.26%

3.13.3 Members discussed at the July meeting a cash flow projection that showed our investment peaking by the end of 2014 at \$23m out of the initial investment of \$40m. In order to maintain our investment level it will be necessary to commit to another fund to recycle the distributions received. Members agreed to invite Franklin Templeton to present at the September meeting to discuss further the cash flow projections and performance to date.

3.13.4 Members are asked to receive the fund manager's presentation and consider the proposal to reinvest the distributions by committing to Fund 2.

3.13.5 If agreement is reached to invest in Fund 2 then delegate to Director of Finance and Director of Legal to undertake due diligence and agree terms.

3.14. **Legal and General**

3.14.1 This is the fund's passive overseas equity index manager. The fund inception date was 8 June 2011 with an initial investment of £67million funded from transfer of assets from AllianzGI (RCM). The funds are managed passively against regional indices to formulate a total FTSE All World Index series. The portfolio returned 4.6% net of fees against a benchmark of 4.7% for the quarter with a 12 months relative return -0.5%. The 3 year absolute return is 1.2% with a market value of £71.6m.

3.15 **Hearthstone**

3.15.1 This is the fund's residential UK property manager. The fund inception date was 23 January 2013, with an initial investment of £20million funded by withdrawals from our equities portfolios. The agreed mandate guidelines are as follows:

- Target performance: UK HPI + 3.75% net income.
- Target modern housing with low maintenance characteristics, less than 10 years old.
- Assets subject to development risk less than 5% of portfolio.
- Regional allocation seeks to replicate distribution of UK housing stock based on data from Academics. Approximately 45% London and South East.
- 5-6 locations per region are targeted based on qualitative and quantitative assessments and data from Touchstone and Connells.
- Preference is for stock which can be let on Assured Shorthold Tenancies (ASTs) or to companies.
- Total returns expected to be between 6.75% and 8.75% p.a., with returns split equally between income and capital growth. Net yields after fund costs of 3.75% p.a.
- The fund benchmark is the LSL Academics House Price Index

- 3.15.2 For the June quarter the value of the fund investment was £21.8m and total funds under management are £29.9million. Performance net of fees was 2.6% compared to the benchmark of 2.1%, and 12 month relative return -3.5%. The income yield after cost was 5.7%. The portfolio had 125 properties, 74 were let on licence and leaseback agreement to house builders and 51 properties let on assured short term agreements. 4 properties have received notices to vacate in July and August and 2 of these have been pre let.

4. Implications

4.1 Financial implications:

The fund actuary takes investment performance into account when assessing the employer contributions payable, at the triennial valuation.

4.2 Legal Implications:

As the administering authority for the Fund, the Council must review the performance of the Fund investments at regular intervals and review the investments made by Fund Managers quarterly.

4.3 Equality Impact Assessment:

The Council must, in carrying out its functions, have due regard to the need to eliminate unlawful discrimination and harassment and to promote equality of opportunity in relation to disability, race and gender and the need to take steps to take account of disabilities, even where that involves treating the disabled more favourably than others (section 49A Disability Discrimination Act 1995; section 71 Race Relations Act 1976; section 76A Sex Discrimination Act 1975."

An equalities impact assessment has not been conducted because this report is an update on performance of existing fund managers and there are no equalities issues arising.

4.4 Environmental Implications

None applicable to this report.

5. Conclusion and reasons for recommendations

- 5.1 Members are asked to note the performance of the fund for the quarter ending June 2014 as part of the regular monitoring of fund performance and receive presentations from Aviva and Franklin Templeton.

Background papers:

1. Quarterly management reports from the Fund Managers to the Pension Fund.
2. Quarterly performance monitoring statistics for the Pension Fund – WM Company

Final report clearance:

Signed by:

Corporate Director of Finance and Resources Date
Received by:

Head of Democratic Services Date

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APPENDIX 1

Summary of Long Term Returns

LONDON BOROUGH OF ISLINGTON - TOTAL COMBINED
 Benchmark - LOCAL AUTHORITY UNIVERSE

Periods to end June
 2014
 Pound Sterling

This page summarises the long term returns at asset class level
 A ranking against the peer group is shown in brackets.

Return %	----- 2011 - -----		----- 2012 ----- -----				----- 2013 ----- -----				----- 2014 - -----		1yr	3yrs % pa	5yrs % pa
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
Total Equity	-13.2 (8)	7.3 (38)	8.1 (64)	-3.1 (18)	5.2 (10)	2.4 (90)	10.9 (97)	-0.6 (67)	4.3 (19)	4.6 (75)	0.1 (56)	2.9 (2)	12.4 (18)	9.2 (38)	13.9 (66)
Private Eq	2.4	-4.5	0.1	1.2	-1.1	-0.3	3.7	6.9	0.6	-1.6	2.6	0.6	2.3	3.5	7.8
UK Equities	-13.3 (43)	8.8 (24)	6.2 (58)	-2.1 (14)	4.5 (77)	3.9 (44)	10.8 (39)	-1.7 (75)	5.5 (74)	5.5 (56)	-0.3 (28)	2.3 (31)	13.6 (46)	9.6 (51)	15.2 (48)
O/S EQ Hedge	-15.8	7.9	12.3	-5.0	7.3	1.0	12.3	-0.4	3.5	4.6	0.1	4.0	12.7	9.8	13.2
O/S Equities	-16.0 (46)	7.1 (22)	10.7 (20)	-3.4 (12)	5.1 (16)	1.9 (93)	13.8 (53)	-1.1 (73)	1.3 (63)	3.7 (70)	-0.2 (82)	3.0 (13)	8.0 (72)	7.8 (59)	12.9 (69)
N. America	-13.5 (65)	11.4 (49)	11.4 (16)	-0.6 (16)	4.8 (14)	-2.3 (96)	19.2 (15)	2.8 (37)	1.0 (16)	8.6 (12)	0.8 (85)	2.3 (55)	13.0 (21)	14.8 (18)	18.5 (16)
Europe ex UK	-19.7 (12)	6.7 (6)	9.4 (68)	-3.0 (6)	7.6 (19)	5.4 (86)	14.2 (21)	1.5 (20)	4.1 (84)	5.9 (32)	0.8 (91)	1.7 (18)	13.2 (67)	10.6 (11)	13.9 (29)
Japan	-5.8	-3.2	9.4	-3.2	-1.6	1.4	22.6	7.8	3.9	-4.0	-5.6	3.2	-2.8	7.4	6.1
MGJE	-3.1	-3.6	8.0	-5.5	-3.5	5.0	19.5	4.4	0.3	0.0	-5.9	4.2	-1.6	5.9	
Pacific	-14.5 (8)	3.2 (85)	11.0 (26)	-5.5 (75)	6.1 (80)	3.7 (80)	8.7 (81)	-9.0 (48)	0.3 (68)	-4.8 (92)	-2.7 (90)	2.6 (44)	-4.7 (94)	-1.4 (91)	6.0 (100)
Other Intl.	-20.8 (72)	4.8 (50)	10.8 (52)	-7.6 (63)	5.3 (36)	5.3 (33)	5.7 (64)	-8.9 (84)	-1.2 (63)	-1.8 (85)	-0.8 (54)	5.3 (9)	1.3 (62)	-2.8 (79)	10.1 (42)
Bonds + IL	0.6 (97)	2.8 (89)	3.4 (2)	2.1 (47)	6.2 (2)	2.7 (38)	1.8 (76)	-2.8 (20)	2.5 (6)	0.4 (17)	2.8 (36)	2.3 (12)	8.2 (10)	8.4 (20)	8.8 (32)
Total Bonds	0.6 (91)	2.8 (76)	3.4 (5)	2.1 (66)	6.2 (8)	2.7 (16)	1.8 (46)	-2.8 (25)	2.5 (11)	0.4 (16)	2.8 (30)	2.3 (17)	8.2 (12)	8.4 (26)	9.0 (32)
UK Bonds	0.6 (93)	2.8 (82)	3.4 (2)	2.1 (69)	6.2 (10)	2.7 (13)	1.8 (27)	-2.8 (18)	2.5 (14)	0.4 (17)	2.8 (30)	2.3 (17)	8.2 (13)	8.4 (27)	9.7 (22)
UK Corp Bond	0.6 (67)	2.8 (55)	3.4 (21)	2.1 (52)	6.2 (32)	2.7 (25)	1.8 (38)	-2.8 (18)	2.5 (37)	0.4 (18)	2.8 (38)	2.3 (41)	8.2 (29)	8.4 (41)	10.4 (35)
Cash/ Alts	1.0 (22)	-0.0 (44)	-1.1 (92)	0.6 (32)	0.2 (53)	0.1 (69)	1.0 (71)	2.5 (19)	0.1 (27)	0.2 (56)	0.6 (55)	0.3 (50)	1.2 (58)	1.8 (55)	5.6 (29)
Cash	1.0 (17)	-0.0 (51)	-1.1 (95)	0.6 (22)	0.2 (34)	0.1 (39)	1.0 (27)	2.5 (16)	0.1 (21)	0.2 (25)	0.6 (19)	0.3 (22)	1.2 (22)	1.8 (17)	-1.1 (100)

Curr Instr	-13.1	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
	(37)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
UK Property	1.6	1.5	1.1	0.6	0.5	1.3	0.7	1.8	1.7	3.2	2.6	3.9	11.8	6.9	8.0	
	(33)	(28)	(19)	(25)	(28)	(18)	(64)	(44)	(78)	(80)	(78)	(72)	(88)	(66)	(77)	
Gbl Property	2.3	0.2	-7.0	6.5	-11.5	-0.8	5.2	5.3	-7.9	3.7	1.4	20.7	16.8	4.8		
FRANKLIN TEM	1.0	0.2	-4.7	3.8	-8.1	0.0 #										
FRANKLIN TEM	2.5	0.2	-7.4	6.9	-12.1	0.0 #										
FRANKLIN TEM						-0.8 #	5.2	5.3	-7.9	3.7	1.4	20.7	16.8			
Total Assets	-8.6	5.5	6.1	-1.5	4.7	2.3	7.5	-0.7	3.4	3.5	0.9	2.9	11.2	8.6	12.1	
	(33)	(57)	(22)	(30)	(4)	(72)	(89)	(43)	(14)	(57)	(55)	(4)	(14)	(26)	(43)	

not invested in this area for the entire period