

COMMITTEE: Pensions Committee	DATE: 19September2013	CLASSIFICATION: Unrestricted	REPORT NO.	AGENDA NO.
REPORT OF: Interim Corporate Director of Resources		TITLE: Report of Investment Panel for Quarter Ending 31 March 2013.		
ORIGINATING OFFICER(S): Paul Thorogood –Interim Service Head, Finance and HR Development Oladapo Shonola – Chief Financial Strategy Officer		Ward(s) affected: N/A		

Lead Member	Cllr Alibor Choudhury - Resources
Community Plan Theme	All
Strategic Priority	One Tower Hamlets

1. SUMMARY

- 1.1 This report informs Members of the activities of the Investment Panel and the performance of the Fund and its investment managers for the period ending 31 March 2013.
- 1.2 In the quarter to the end of March 2013 the Fund achieved a return of 9.0% which is 0.8% above the benchmark 8.2%. The twelve month Fund return of 12.0% exceeds the benchmark by 1.1% at 10.9%. Over the longer term, performance is ahead of the benchmark with three year returns of 6.8% being 0.2% above the benchmark and the five year returns of 5.8% exceeding the benchmark by 0.1%.
- 1.3 The latest performance figures shows that performance is heading in the right direction and for the first time in several years, the Fund is now ahead of benchmark over all time periods. This is as a result of a combination of market recovery, especially equities, and strategic decisions made by the Investment Panel on new allocations and appointment of investment managers.
- 1.4 Seven out of eight managers matched or achieved returns above the benchmark with the diversified growth and absolute return investments exceeding the benchmark by 5% and 10% respectively. GMO continued to lag the benchmark however this does partially reflect the management structure of the fund where complementary investment styles are used to reduce the volatility of overall portfolio returns.
- 1.5 The Fund is still in line with its long term strategic equity asset allocation and the distribution of the Fund's assets amongst the different asset classes is broadly in line with benchmark.

2. DECISIONS REQUIRED

- 2.1 Members are recommended to note the contents of this report.

3. REASONS FOR DECISIONS

3.1 There are no decisions to be made as a result of this report. The report is written to inform committee members of the performance of pension fund managers and the overall performance of the Tower Hamlets Pension Fund.

4. ALTERNATIVE OPTIONS

4.1 The Pension Fund Regulations require that the Council establishes arrangements for monitoring the investments of the Pension Fund.

5. BACKGROUND

5.1 The Pension Fund Regulations require that the Council establish arrangements for monitoring the investments of the Fund and the activities of the investment managers and ensure that proper advice is obtained on investment issues.

5.2 This Committee has established the Investment Panel, which meets quarterly for this purpose. The Panel's membership comprises all Members of the Pensions Committee, an Investment Professional as Chair, an Independent Investment Adviser, and the Corporate Director of Resources represented by the Service Head Financial Services, Risk and Accountability, one trade union representatives and one representative of the admitted bodies. The Investment Panel is an advisory body which makes recommendations to the Pensions Committee which is the decision making body.

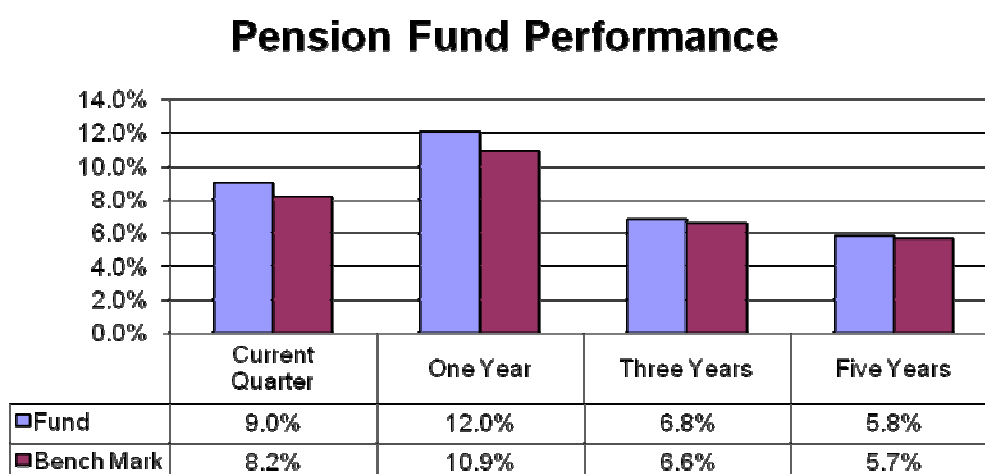
5.3. Officers and fund advisers meet regularly with investment managers to discuss their strategy and performance and may recommend that investment managers are invited to explain further to the Investment Panel.

6 INVESTMENT PERFORMANCE

6.1 The Fund achieved a return of 9.0% in the quarter which is 0.8% above the benchmark of 8.2%.

6.2 The performance of the fund over the longer term is as set out in table 1.

Table 1 – Fund Performance



6.3 The chart demonstrates the volatility and cyclical nature of financial markets, but the outcomes are within the range of expectations used by the Fund actuary in assessing the funding position. The Fund can take a long term perspective on investment issues principally because a high proportion of its pension liabilities are up to sixty years in the future. Consequently it can effectively ride out short term volatility in markets.

7. MANAGERS

7.1 The Fund currently employs eight specialist managers with mandates corresponding to the principal asset classes. The managers, mandate and funds held under management are set out below:

Table 2: Management Structure

Manager	Mandate	Value £M	Target % of Fund	Actual % of Fund	Difference %	Date Appointed
GMO	Global Equity	227.5	25.0%	24.4%	-0.6%	29 Apr 2005
Baillie Gifford	Global Equity	163.1	16.0%	17.5%	1.5%	5 Jul 2007
L & G UK Equity	UK Equity	194.6	20.0%	20.9%	0.9%	2 Aug 2010
Baillie Gifford Diversified Growth	Absolute Return	46.3	5.0%	5.0%	0.0%	22 Feb 2011
Ruffer Total Return Fund	Absolute Return	45.5	5.0%	4.9%	-0.1%	8 Mar 2011
L & G Index Linked- Gilts	UK Index Linked	51.4	3.0%	5.5%	2.5%	2 Aug 2010
Investec Bonds	Bonds	97.0	14.0%	10.4%	-3.6%	26 Apr 2010
Schroder	Property	95.8	12.0%	10.3%	-1.7%	30 Sep 2004
Cash	Currency	9.7	0.0%	1.0%	1.0%	
Total		930.9	100.0%	100.0%	0.0%	

7.2 The fund value of £930.9 million as at 31 March 2013, which includes cash held, has increased by £76.4million (8.94%) over the quarter.

7.3 The performance of the individual managers relative to the appropriate benchmark over the past five years is as set out in table 3.

Table 3: Manager Investment Performance relative to benchmark

Manager	Current Quarter	One Year	Three Years	Five Years
GMO	-2.10%	-3.30%	-1.10%	-0.80%
Baillie Gifford	1.50%	2.20%	2.50%	2.30%
L & G UK Equity	0.10%	0.10%	0.20%	N/A
Baillie Gifford Diversified Growth	5.00%	10.90%	7.20%	N/A
Ruffer Total Return Fund	10.00%	10.20%	5.50%	N/A
L & G Index Linked-Gilts	0.00%	0.00%	0.00%	N/A
Investec Bonds	0.00%	1.20%	-1.20%	N/A
Schroder	0.30%	0.10%	-1.10%	-1.20%
Total Variance (Relative)	0.10%	0.00%	-0.30%	-0.40%

- 7.4 **GMO** underperformed benchmark this quarter, delivering returns of 11.4% which was 2.1% below benchmark of 13.8%. Global equity markets rallied in the first quarter of 2013 and although GMO made positive returns from their US quality holdings, this was offset by negative returns from their European value holdings which were adversely affected by events in Italy and Cyprus. However, GMO believe there are good returns to be had in the future by taking advantage of the very low stock market pricing in Europe where high quality companies are trading at the lowest valuations in recent decades.
- 7.5 **Baillie Gifford Global Alpha Fund** delivered returns of 15.9% outperforming benchmark by 1.5% in this quarter. The portfolio continued to perform strongly with the highest regional returns coming from North America and Developed Asia. The main contributors to performance were Svenska Handelsbanken (a Swedish bank who are expanding their branch network in the UK and Netherlands), Prudential and Mindray (a medical equipment manufacturer).
- 7.6 **L & G (UK Equity)** performance has been in line with the index benchmark (FTSE-All Share) since inception, as expected.
- 7.7 **L & G Index Linked Gilts** performance has been in line with the index benchmark (FTSE-A Index-Linked Over 15 Years Gilts) since inception.
- 7.8 **Investec (Bonds)** – The fund returned 0.2% against a benchmark of 0.1%. The main contributor to outperformance was currency positioning through a bias to the US dollar, Yen and Sterling. The exposure to emerging market bonds also contributed to performance. Investec believe smaller core government bonds (Sweden, Norway, New Zealand and Australia) offer best value as they continue to avoid peripheral Eurozone debt.
- 7.9 **Schroder (Property)** achieved returns of 1.1% against a benchmark of 0.8%, outperforming its benchmark by 0.3%. However, performance over the three and five years remained below benchmark at 1.1% and 1.2% respectively. The fund's strategy of targeting an overweight position to central London offices has delivered most of the outperformance. The European fund meanwhile continues to be a drag on returns but Schroders anticipate this will improve in the future.
- 7.10 **Baillie Gifford Diversified Growth Fund** delivered a return of 5.1% this quarter against a benchmark of 0.1%, which equates to a strong outperformance of 5.0%. Listed equities and emerging market bonds contributed significantly to this quarter's outperformance as the portfolio has a significant allocation to these markets. The fund continues to perform strongly as it has done since inception.
- 7.11 **Ruffer Total Return Fund (Absolute Return)** the fund posted strong figures for Q4 delivering returns of 10.1% against a benchmark of 0.1%, which equates to a relative outperformance of 10.0%. Equities and index-linked gilts were the main contributors to outperformance while the falling price of gold detracted from it. The fund continues to perform strongly as it has done since inception.

8 **ASSET ALLOCATION**

8.1 The original allocation of investments between the different asset classes was determined in conjunction with the Council's professional advisors in 2004 and is subject to periodic review by the Investment Panel – the latest review was carried out in January 2011. Asset allocation is determined by a number of factors including:-

8.1.1 The risk profile. Generally there is a trade-off between the returns obtainable on investments and the level of risk. Equities have higher potential returns but this is achieved with higher volatility. However, as the Fund remains open to new members and able to tolerate this it can seek long term benefits of the increased returns.

8.1.2 The age profile of the Fund. The younger the members of the Fund, the longer the period before pensions become payable and investments have to be realised for this purpose. This enables the Fund to invest in more volatile asset classes because it has the capacity to ride out adverse movements in the investment cycle.

8.1.3 The deficit recovery term. All Council funds are in deficit because of falling investment returns and increasing life expectancy. The actuary determines the period over which the deficit is to be recovered and considers the need to stabilise the employer's contribution rate. The actuary has set a twenty year deficit recovery term for this Council which enables a longer term investment perspective to be taken.

8.2 The benchmark asset distribution and the position at the 31 March 2013 are as set out below:

Table 4: Asset Allocation

Mandate	Benchmark 31 Mar 2013	Fund Position	Variance as at 31 Mar 2013	Variance as at 31 Mar 2012
UK Equities	20.0%	20.9%	0.9%	0.0%
Global Equities	41.0%	42.0%	1.0%	-0.4%
Total Equities	61.0%	62.9%	1.9%	-0.4%
Property	12.0%	10.3%	-1.7%	-0.5%
Bonds	14.0%	10.4%	-3.6%	-2.5%
UK Index Linked	3.0%	5.5%	2.5%	2.5%
Alternatives	10.0%	9.9%	-0.1%	0.0%
Cash	0.0%	1.0%	1.0%	0.9%
Currency	0.0%	0.0%	0.0%	0.0%
Total Equities	100.0%	100.0%		

8.3 Allocations are therefore considered to be broadly in line with the benchmark. Individual managers have discretion within defined limits to vary the asset distribution.

9. COMMENTS OF THE CHIEF FINANCIAL OFFICER

- 9.1. The comments of the Corporate Director Resources have been incorporated into the report.

10. CONCURRENT REPORT OF THE ASSISTANT CHIEF EXECUTIVE (LEGAL)

- 10.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 require the Council, as an administering authority, to invest fund money that is not needed immediately to make payments from the Pensions Fund. The Council is required to have a policy in relation to its investments and a Statement of Investment Principles. The Council is required to take advice about its investments.
- 10.2 The Council does not have to invest the fund money itself and may appoint one or more investment managers. Where the Council appoints an investment manager, it must keep the manager's performance under review. At least once every three months the Council must review the investments that the manager has made and, periodically, the Council must consider whether or not to retain that manager.
- 10.3 One of the functions of the Pensions Committee is to meet the Council's duties in respect of investment matters. It is appropriate, having regard to these matters, for the Committee to receive information about asset allocation and the performance of appointed investment managers.

11. ONE TOWER HAMLETS CONSIDERATIONS

- 11.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.
- 11.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

12. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

- 12.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

13. RISK MANAGEMENT IMPLICATIONS

- 13.1 Any form of investment inevitably involves a degree of risk.
- 13.2 To minimise risk the Investment Panel attempts to achieve a diversified portfolio. Diversification relates to asset classes and management styles.

14. CRIME AND DISORDER REDUCTION IMPLICATIONS

- 14.1 There are no crime and disorder reduction implications arising from this report.

15. EFFICIENCY STATEMENT

- 15.1 The monitoring arrangement for the Pension Fund and the work of the Pension Fund Investment Panel should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

LOCAL GOVERNMENT ACT 1972 (AS AMENDED) SECTION 100D

LIST OF "BACKGROUND PAPERS" USED IN THE PREPARATION OF THIS REPORT

<i>Brief description of "background papers"</i>	<i>Name and telephone number of holder And address where open to inspection</i>
<i>None</i>	