

## Regulatory and Other Committee

### Open Report on behalf of Executive Director of Finance and Public Protection

Report to:	<b>Pensions Committee</b>
Date:	<b>16 July 2015</b>
Subject:	<b>Investment Management Report</b>

#### Summary:

This report covers the management of the Lincolnshire Pension Fund assets, over the period from 1st January to 31st March 2015.

#### Recommendation(s):

That the committee note this report.

### Background

This report is split into four areas:

- Funding Level Update
- Fund Performance & Asset Allocation
- Hymans Robertson Manager Ratings
- Individual Manager Update

#### 1. Funding Level Update

1.1 The funding update is provided to illustrate the estimated development of the funding position from 31<sup>st</sup> March 2013 to 31<sup>st</sup> March 2015, for the Fund.

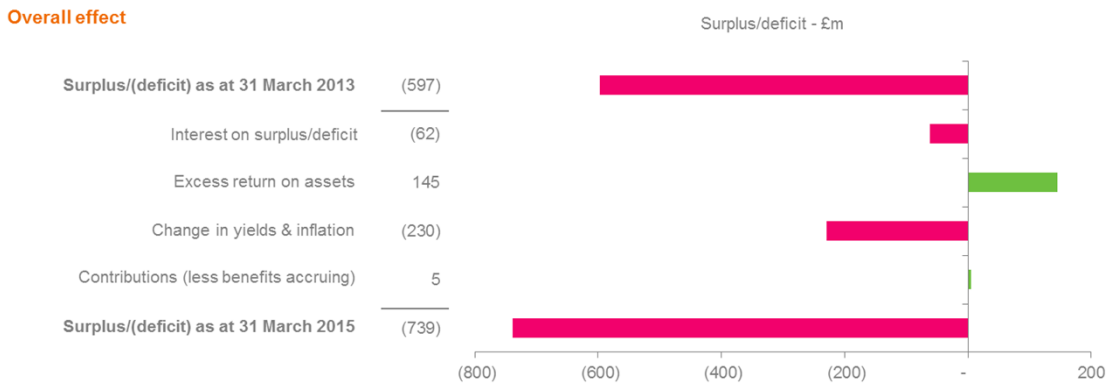
1.2 As the graph below shows, the funding level at the latest formal valuation was 71.5%. As at 31<sup>st</sup> March 2015 the funding level has decreased to 70.5%.

Change in funding level since last valuation



1.3 As shown below, the deficit in real money has increased from £597m to £739m between the period 31<sup>st</sup> March 2013 and 31<sup>st</sup> March 2015. This is largely as a result of a decrease in bond yields, and subsequent discount rate, which places a higher value on the Fund's liabilities. This has been partially offset by good investment performance.

What's happened since last valuation?



1.4 In the period since 31<sup>st</sup> December 2014, the funding level has risen from 70% to 70.5% as a result of good investment performance.

**2. Fund Performance & Asset Allocation**

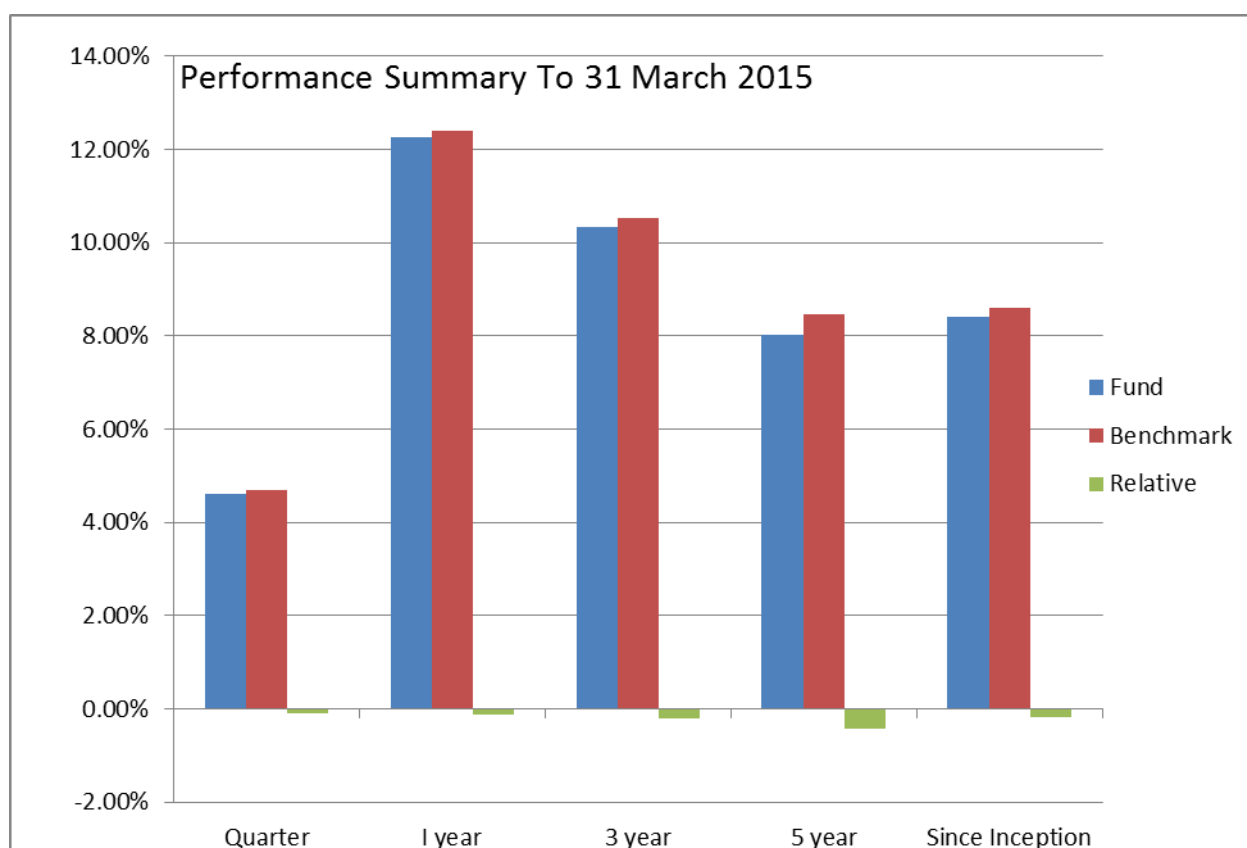
2.1 The Fund increased in value by £81.9m during the quarter from £1,669.8m to £1,751.7.8m, as the chart below shows. The Fund was

overweight to cash and global equities and underweight UK equities, fixed interest, alternatives and property.

Asset Class	Q1 2015 £	Q4 2014 £	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	348.1	314.8	19.9	20.0	(0.1)
Global Equities	725.7	719.1	41.4	40.0	1.4
Alternatives	248.2	236.3	14.2	15.0	(0.8)
Property	193.5	190.2	11.0	11.5	(0.5)
Fixed Interest	228.6	206.5	13.1	13.5	(0.4)
Cash	7.6	2.8	0.4	0.0	0.4
<b>Total</b>	<b>1,751.7</b>	<b>1,669.8</b>	<b>100.0</b>	<b>100.0</b>	

2.2 The graph below shows the Fund's performance against the benchmark over the quarter, one year, three years, five years and since inception. The Fund has a target to outperform the strategic benchmark by 1% per annum.

2.3 Over the quarter, the Fund produced a positive return of 4.6% underperforming the benchmark which returned 4.69%. The Fund is behind the benchmark over all other periods.



\* Since Inception figures are from March 1987

### 3. Hymans Robertson Manager Ratings

3.1 Hymans Robertson regularly meet managers to discuss current issues, management changes and performance. The manager is then allocated one of five ratings between replace and retain. The table below shows Hymans Robertson's rating of all managers that have been appointed by the Lincolnshire Pension Fund.

3.2 The Fund has twenty managers and there have been no changes to the ratings during the quarter. Sixteen managers remained rated as retain and four managers, Rreef Property Ventures Fund 3, Aviva Pooled Property Fund, Neptune and Schroders, as "on watch". Officers will monitor these managers closely and arrange meetings to discuss any potential issues

### 3.3

Manager	Rating			
	Replace		On Watch	Retain
Invesco Global Equities (Ex-UK)				X
Threadneedle Global Equity				X
Schroders Global Equity			X	
Neptune Global Equity			X	
Morgan Stanley Global Brands				X
F&C Absolute Return Bonds				X
Morgan Stanley Alternative Investments				X
Blackrock Fixed Interest				X
Standard Life European Property				X
Innisfree Continuation Fund 2				X
Innisfree Secondary Fund				X
Innisfree Secondary Fund 2				X
Franklin Templeton European Real Estate				X
Franklin Templeton Asian Real Estate				X
RREEF Ventures Fund 3			X	
Igloo Regeneration Partnership				X
Aviva Pooled Property Fund			X	
Royal London PAIF				X
Standard Life Pooled Property Fund				X
Blackrock Property				X

## 4. Individual Manager Update

4.1 The manager returns and index returns for equity, fixed interest and alternative managers are shown in the table below. A detailed report on each manager outlining the investment process, performance, purchases and sales and Hymans Robertson's manager view can be found after the table at 4.2.

4.2 Manager Returns – As shown below it was a good quarter for the Fund with all managers producing a positive absolute return. Over the quarter, six managers outperformed their benchmark, with the in house team slightly underperforming by 0.1% and Morgan Stanley Global Brands and Alternatives underperforming by 1.6% and 0.7%. Over the 12 month period only F&C have failed to produce a positive absolute return. Against their target, the

performance has been disappointing with only the in house team and Blackrock matching or beating the required return.

	3 months ended 31/03/15			Previous 12 months			
Manager	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	Target p.a. %
Passive UK Equity In house	4.3	4.5	(0.1)	5.6	5.8	(0.2)	+/- 0.5
Invesco (Global Equities (ex UK))	8.0	7.8	0.2	20.2	20.3	(0.1)	+1.0
Threadneedle (Global Equities)	8.2	7.6	0.5	19.5	19.0	0.4	+2.0
Neptune (Global Equities)	8.7	7.6	1.0	23.0	19.0	3.4	+4.0
Schroder's (Global Equities)	8.7	7.5	1.1	19.7	18.4	1.1	+3.0
Morgan Stanley Global Brands	5.8	7.5	(1.6)	18.4	19.1	(0.6)	n/a
Blackrock (Fixed Interest)	3.3	3.2	0.1	14.5	14.2	0.3	Match Index
F&C (Fixed Interest)	1.4	0.8	0.7	(1.3)	3.1	(4.3)	3M LIBOR + 3%
Morgan Stanley (Alternative Investments)	0.5	1.2	(0.7)	0.1	4.7	(3.5)	3M LIBOR + 4%

**Lincolnshire Pension Fund  
UK Equities – In House (Passive UK)  
Quarterly Report March 2015**

**Investment Process**

This portfolio is managed internally and mandated to track the MSCI UK IMI index +/- 0.5% around the index, with a tracking error of 0.5%. Approximately 250-300 stocks are held.

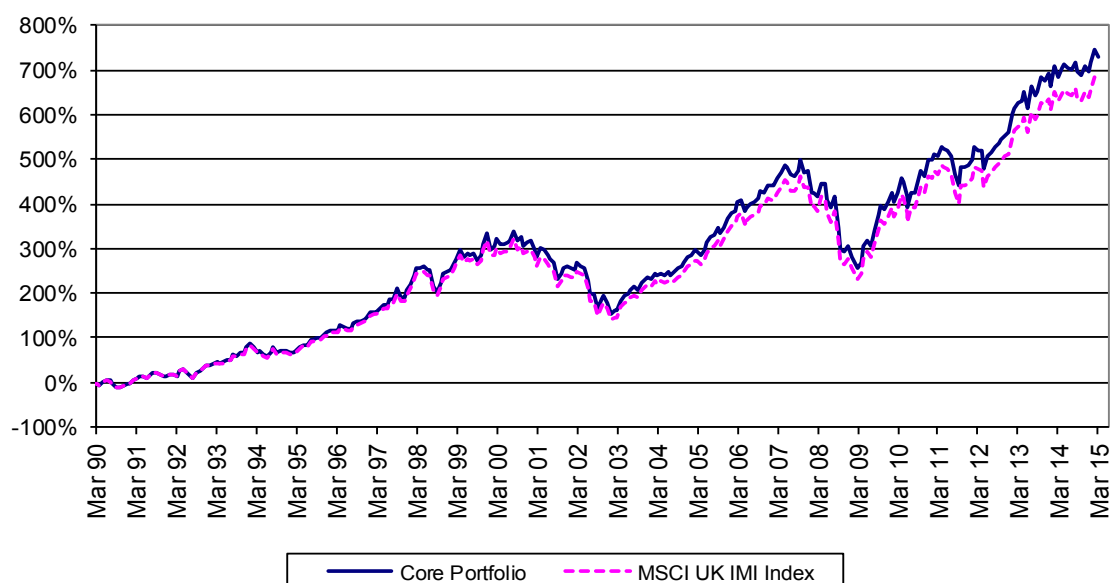
**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£314,780,654	£348,079,334

**Performance**

During the quarter the portfolio produced an excellent return of 4.3% but slightly lagged the benchmark by 0.1%. The underperformance was due to the underweight position in financials which delivered a strong return over the quarter. The portfolio is slightly behind the benchmark over one and three year time periods but ahead over five years and since inception.

**UK Equities In House Portfolio Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
UK Equities – In House	4.3	5.6	14.4	11.0	8.8
MSCI UK IMI	4.5	5.8	14.5	10.9	8.5
Relative Performance	(0.1)	(0.2)	(0.1)	0.1	0.3

\* annualised, inception date 01/10/1989

## Turnover

Holdings at 31.12.14	Holdings at 31.03.15	Turnover in Quarter %	Turnover in Previous Quarter %
248	256	3.7	0.01

## Purchases and Sales

During the quarter the manager performed a large number of trades following a rebalance of the Lincolnshire Pension Fund. Purchases included Lloyds, Barclays and HSBC as the manager continued to reduce the underweight position in financials. The manager sold positions in Punch Taverns, Jardine Lloyd Thompson and Canaccord as these stocks exited the index.

## Largest Overweights

Royal Dutch Shell	0.13%
Babcock Intl	0.13%
BP Group	0.09%
British American Tobacco	0.09%
BG Group	0.09%

## Largest Underweights

London Stock Exchange	(0.10%)
Rotork	(0.10%)
Glencore	(0.06%)
Kier Group	(0.06%)
GW Pharmaceuticals	(0.06%)

\* Measured against MSCI UK IMI

## Top 10 Holdings

1	Royal Dutch Shell	£23,025,947	6	Vodafone Group	£10,520,870
2	HSBC Holdings	£21,485,474	7	Astrazeneca	£9,841,490
3	BP	£15,017,363	8	Diageo	£7,838,433
4	GlaxoSmithkline	£12,780,037	9	Lloyds Banking Group	£7,653,508
5	British American Tobacco	£12,116,729	10	Prudential PLC	£7,366,836

## Risk Control

The portfolio has a tracking error limit of 0.5%. At the end of March 2015 the tracking error was 0.17%.



**Lincolnshire Pension Fund**  
**Global Equities – Invesco (Global Ex UK Enhanced)**  
**Quarterly Report March 2015**

**Investment Process**

This portfolio is mandated to track the MSCI World ex UK Index, with a performance target of +1% and a tracking error of 1%. The aim is to achieve long-term capital growth from a portfolio of investments in large-cap global companies. Active performance is generated through a quantitative bottom-up investment process, driven by stock selection and based on four concepts: Earnings Momentum, Price Trend, Management Action and Relative Value.

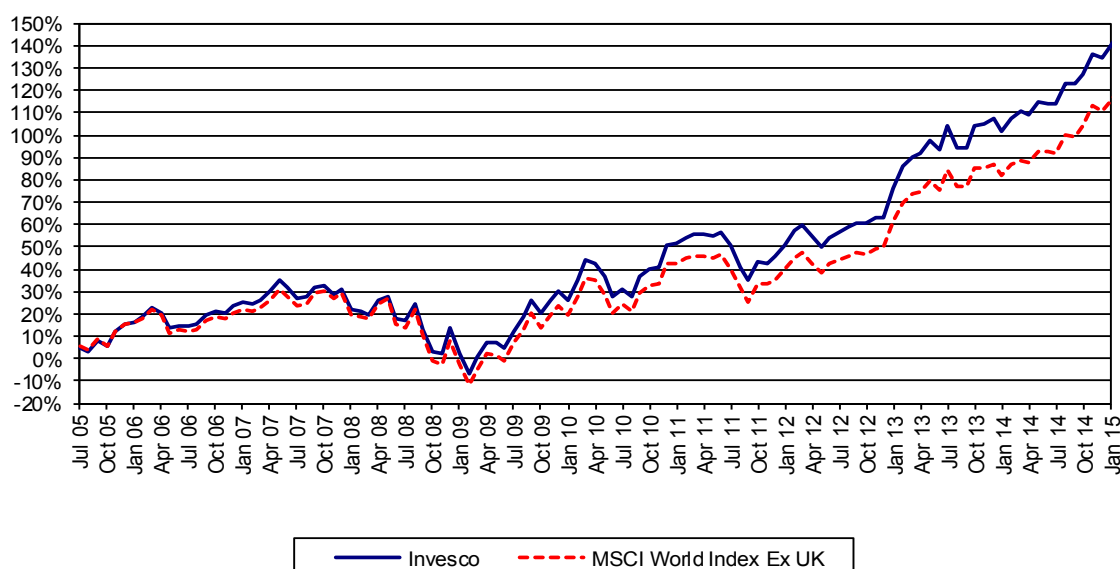
**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£355,830,048	£363,555,873

**Performance**

During the quarter Invesco's strategy outperformed its benchmark. Stock Selection had the largest positive impact on relative performance. An underweight position in materials detracted the most, while underweights in healthcare helped performance. Over 12 months Invesco have slightly underperformed their benchmark but over all other periods they are ahead of both the benchmark and the target.

**Invesco Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	8.0	20.2	16.6	12.0	10.0
MSCI World ex UK	7.8	20.3	15.5	10.8	8.8
Relative Performance	0.2	(0.1)	1.0	1.1	1.1

\* annualised, inception date 1<sup>st</sup> July 2005

## Turnover

Holdings at 31.12.14	Holdings at 31.03.15	Turnover in Quarter %	Turnover in Previous Quarter %
429	419	11.5	8.0

## Purchases and Sales

During the quarter Invesco added Amerisourcebergen and Equity Residential whilst increasing their position in Intel, Abbvie and Comcast. These were funded by selling out of Vinci and Discover Financial and decreasing positions in Chevron, Power Assets and Northrop Grumman.

### Largest Overweights

Pfizer	0.81%
Nippon Tel & Tel	0.81%
Citigroup	0.81%
Archer Daniels Midl	0.75%
Northrop Grumman	0.72%

### Largest Underweights

Chevron	(0.59%)
Verizon	(0.52%)
Google	(0.51%)
Amazon	(0.47%)
Walt Disney	(0.46%)

\* Measured against MSCI World ex UK (NDR)

## Top 10 Holdings

1	Apple Inc	£9,720,223
2	Microsoft Corp	£5,957,983
3	JPMorgan Chase	£5,334,958
4	Pfizer Inc	£5,334,937
5	Citigroup Inc	£4,697,039

6	Johnson & Johnson	£4,596,089
7	Exxon Mobil Corp	£4,042,302
8	Intel Corp	£3,833,773
9	General Electric Co	£3,504,937
10	Nippon Tel & Tel	£3,413,558

## Hymans Robertson View

Karl Georg Bayer is retiring as Head of Research and is being replaced by Michael Fraikin. This will mean Fraikin doing fewer client meetings – his role will be taken by Thorsten Paarmann, another very experienced member of the Portfolio Management team. There will be no change, in our view, to the philosophy, process or portfolio structure resulting from Fraikin's promotion.

## Risk Control

The predicted tracking error of the portfolio decreased to 1% (actual target 1%).

## Lincolnshire Pension Fund Global Equities – Neptune Quarterly Report March 2015

### Investment Process

This portfolio is mandated to outperform the MSCI All Countries World Index by 2% to 4% over rolling three year periods, net of fees. This is achieved through generating capital growth from a concentrated portfolio of global securities, selected from across world equity markets. The investment process of Neptune means that they will usually generate more volatile returns than the Fund's other Global Equity Managers and are seen as benchmark agnostic.

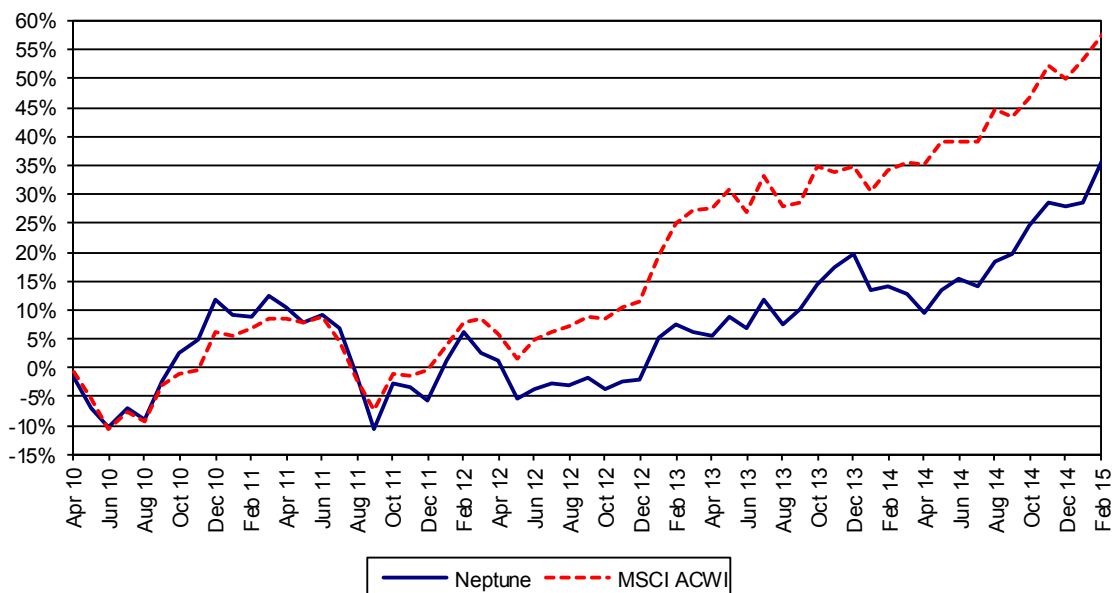
### Portfolio Valuation

Value at 31.12.14	Value at 31.03.15
£89,349,824	£91,900,198

### Performance

During the quarter Neptune produced a positive return of 8.7% against the benchmark of 7.6%. The Fund's strong performance for the quarter was driven by stock selection, with 8 out of 10 sectors showing positive stock selection. Particularly positive were industrials, IT and financials, with the stocks within those sectors predominately in the US and Japan.

#### Neptune Performance Since Inception



	Quarter %	1 Year %	3 Year %	5 Year %	Inception* %
Neptune	8.7	23.0	10.6	6.8	6.8
MSCI ACWI**	7.6	19.0	14.1	10.1	10.1
Relative Performance	1.0	3.4	(3.1)	(3.0)	(3.0)

\* annualised, inception date 16/04/2010

## Turnover

Holdings at 31.12.14	Holdings at 31.03.15	Turnover in Quarter %	Turnover in Previous Quarter %
46	54	17.4	10.4

## Purchases and Sales

The main change to the portfolio over the period was an increase to consumer discretionary exposure. This was primarily in the US, where Neptune believe the Consumer's purchasing ability is a stand out beneficiary of the strong dollar and lower oil price. Additionally, on the back of ongoing internal research reports around the health and wellness sector, Neptune added to consumer staples in the US. Neptune also added to healthcare through the purchase of select biotech stocks. These additions were funded by a combination of stock specific sales where target prices had been reached and the trimming of some large US technology stock holdings.

### Top 5 Contributions to Return

Fanus	1.3%
Tencent Holdings	0.8%
Isetan Mitsukoshi	0.8%
Apple Computer	0.8%
Blackstone Group	0.5%

### Bottom 5 Contributions to Return

Caterpillar Inc	(0.1%)
Microsoft Corp	(0.2%)
ICICI Bank	(0.2%)
Komatsu	(0.2%)
American Express Co	(0.2%)

## Top 10 Holdings

1	Fanuc Corp	£3,966,535
2	Apple Inc	£3,259,086
3	Sumitomo Realty	£3,158,257
4	Mitsui Fudosan	£3,106,857
5	Mitsubishi Estate	£3,074,993

6	Taisei Corp	£2,926,708
7	Linkedin Corp	£2,869,579
8	Icici Bank	£2,842,362
9	Tencent Holdings	£2,699,894
10	Google Inc	£2,678,673

## Hymans Robertson View

Hymans view has not changed following their meeting with Neptune in early 2015 and still retain their "on watch" rating.

## Risk Control

The portfolio may invest up to a maximum of 10% of value in securities outside the benchmark index and, in addition, may hold a maximum of 20% of value in cash, in any currency. The portfolio has no regional constraints but will always maintain exposure to at least seven of the ten MSCI Global Sectors and a broad geographical reach.

**Lincolnshire Pension Fund  
Global Equities – Schroders  
Quarterly Report March 2015**

**Investment Process**

This portfolio is mandated to outperform the MSCI All Countries World Daily Net Index by 2% to 4% over rolling three year periods, gross of fees. This is achieved through an investment approach that is designed to add value relative to the benchmark through both stock selection and asset allocation decisions. Schroders believe that stock markets are inefficient and they can exploit this by undertaking fundamental research and taking a long term view.

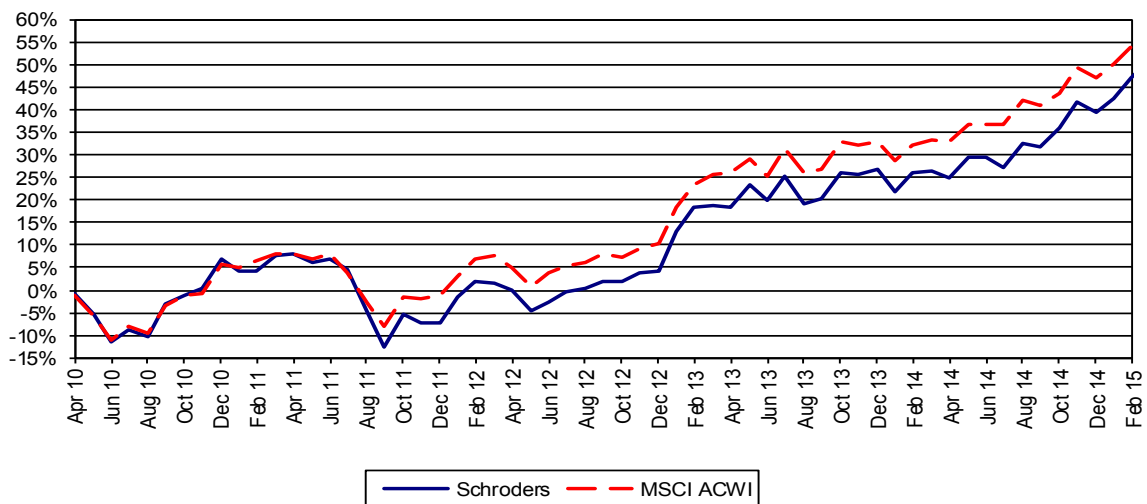
**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£93,108,106	£90,450,362

**Performance**

Schroders outperformed the benchmark over the period as stock selection drove strong relative returns, particularly in North America. Schroder's holdings in the UK were also supportive. Stock selection in Europe and emerging markets detracted from performance. These effects more than offset the negative impact of their positions in the consumer staples and healthcare sectors.

**Schroders Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Schroders	8.7	19.7	14.2	8.7	8.7
MSCI ACWI (Net)	7.5	18.4	13.6	9.6	9.6
Relative Performance	1.1	1.1	0.6	(0.8)	(0.8)

\*annualised since Inception April 16 2010

## Turnover

Holdings at 31.12.14	Holdings at 31.03.15	Turnover in Quarter %	Turnover in Previous Quarter %
67	66	19.4	8.6

## Purchases and Sales

During the quarter Schroders made purchases of Pfizer, Estee Lauder and Apple. These were funded by selling out of eBay and Parker Hannifin and reducing their holding in Hershey.

### Top 5 Contributions to Return

Cognizant Tech Solution	0.3%
United Health Group	0.3%
Bridgestone	0.2%
Pwens Corning	0.2%
Astellas Pharma	0.2%

### Bottom 5 Contributions to Return

Alibaba	(0.2%)
Credit Suisse	(0.2%)
Harley-Davidson	(0.2%)
Citigroup	(0.2%)
Metlife	(0.1%)

## Top 10 Holdings

1	Taiwan Semiconductor	£2,554,919	6	SMC Corp	£2,051,126
2	Pfizer Inc	£2,330,244	7	Apple Inc	£1,949,830
3	Citigroup Inc	£2,329,544	8	US Bancorp	£1,921,537
4	Google Inc	£2,134,009	9	Sumitomo Mitsui Fin	£1,912,162
5	BBVA	£2,110,862	10	Amgen Inc	£1,887,882

## Hymans Robertson View

Hymans rate Schroders as "on watch". They are optimistic that Schroder's fundamental equity team has been successfully refocused under the leadership of Alex Tedder and Hymans will be reviewing their "on watch" during Q3 2015 at which stage Tedder will have been in his role for 12 months.

## Risk Control

The portfolio can have a maximum 10% off-benchmark exposure; any increase in this would require the consent of the Pension Fund.

**Lincolnshire Pension Fund  
Global Equities – Threadneedle  
Quarterly Report March 2015**

**Investment Process**

This portfolio is mandated to outperform the MSCI All Countries World Index by 2% per annum, gross of fees over rolling three year periods. This is achieved through investment managers who can draw on their own knowledge and that of other parts of the organisation to implement a thematic approach to stock selection.

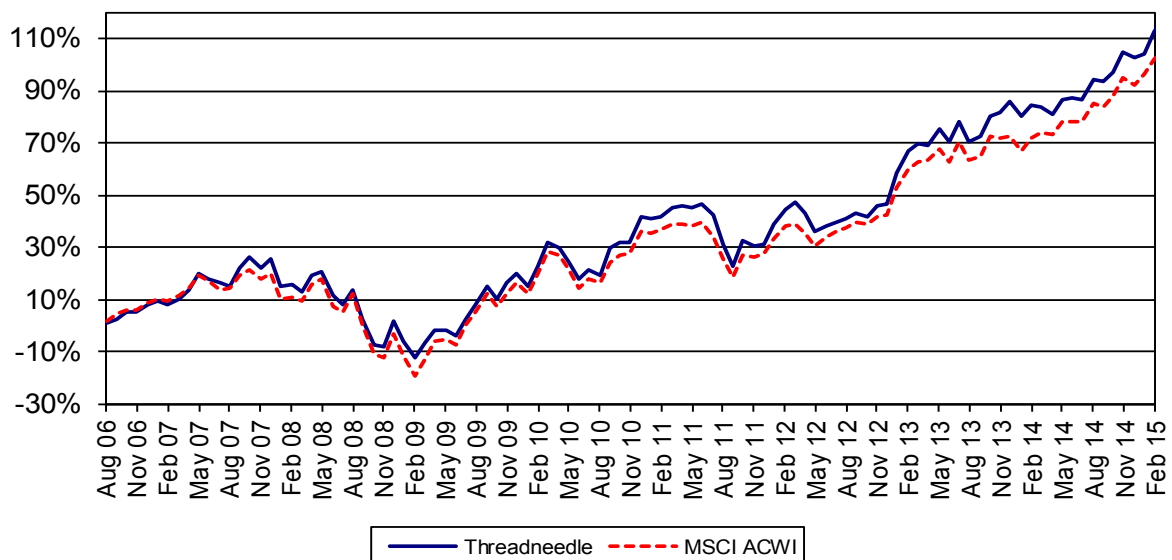
**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£97,217,115	£91,378,618

**Performance**

Threadneedle outperformed its benchmark in the quarter. Regional allocation detracted as Europe ex UK, where they are underweight, outperformed. At a sector level Threadneedle benefitted from its underweight position in energy and utilities, which underperformed. Performance over all periods is above the benchmark but lags the target of 2% outperformance.

**Threadneedle Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Threadneedle	8.2	19.5	14.3	10.7	9.5
MSCI ACWI	7.6	19.0	14.3	10.0	8.7
Relative Performance	0.5	0.4	0.2	0.6	0.7

\* annualised, inception date 01/08/2006

## Turnover

Holdings at 31.12.14	Holdings at 31.03.15	Turnover in Quarter %	Turnover in Previous Quarter %
87	86	15.0	8.5

## Purchases and Sales

Threadneedle opened a position in Towers Watson, Inditex and Tencent. They reduced their position in Praxair and exited their position in Hewlett Packard.

### Top 5 Contributions to Return

Apple Inc	0.5%
Japan Exchange Group	0.4%
Ping An Ins group	0.4%
Walt Disney Co	0.4%
Novo Nordisk	0.3%

### Bottom 5 Contributions to Return

Mazda Motor Co	(0.2%)
American Express Co	(0.2%)
Alibaba Grp Hldgs	(0.2%)
WESCO Intl Inc	(0.1%)
Hertz Global Hlgs	(0.1%)

## Top 10 Holdings

1	Apple Inc	£2,379,051
2	Ping An Ins Group	£2,234,515
3	Walt Disney Co	£2,028,160
4	Express Scripts Hldg	£1,898,579
5	Gilead Sciences	£1,857,677

6	Aon PLC	£1,816,152
7	Comcast Corp	£1,762,591
8	Anheuser Busch	£1,752,569
9	UBS AG	£1,729,764
10	Amphenol Corp	£1,716,785

## Hymans Robertson View

Hymans rate Threadneedle as "retain". Personnel turnover has ceased under William Davies who transferred from the successful European team at the end of 2011.

## Risk Control

The portfolio can have a maximum 10% off-benchmark exposure; any increase in this would require the consent of the Pension Fund.



**Lincolnshire Pension Fund  
Global Equities – Morgan Stanley Global Brands  
Quarterly Report March 2015**

**Investment Process**

The Global Brands Fund is an open-ended investment company incorporated in the United Kingdom. The aim of the Fund is to provide long term capital appreciation through investing in a concentrated high quality global portfolio of companies with strong “intangible assets”. The Fund is benchmarked against the MSCI World Index. Managers aim to gain an absolute return to the Fund rather than a relative return against their benchmark index.

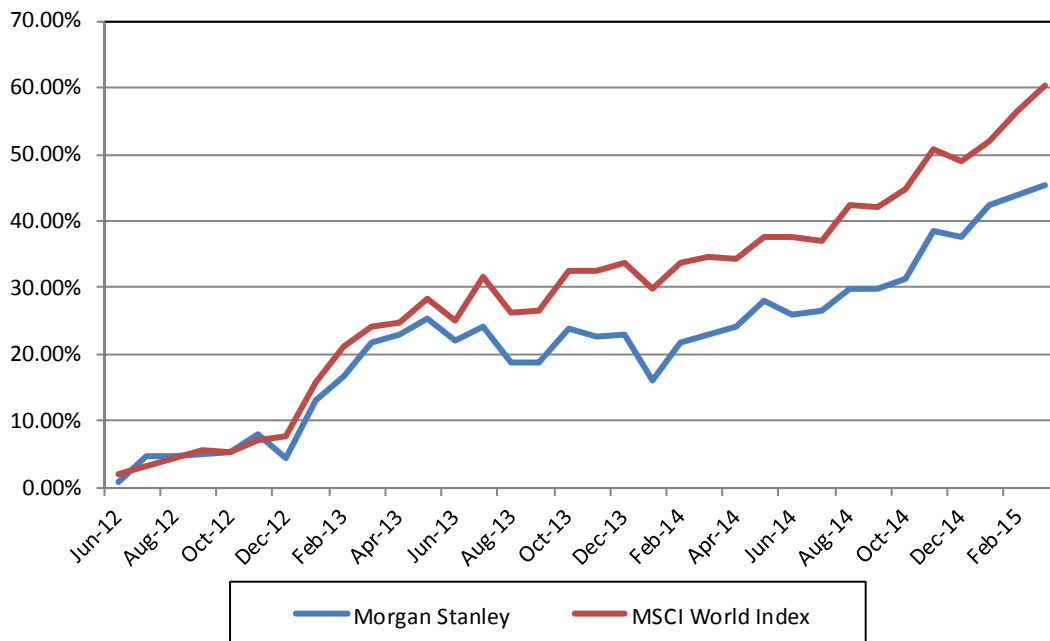
**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£83,622,490	£88,445,435

**Performance**

During the quarter Morgan Stanley Global Brands returned 5.8% underperforming its benchmark by 1.6%. The underperformance for the quarter was mainly due to their stock selection in consumer staples and information technology. Morgan Stanley's allocation to healthcare and stock selection in consumer discretionary also detracted from relative performance. The portfolio's zero weights in energy and utilities, and the allocation to and stock selection in financials were positive contributors for the period.

**Morgan Stanley Global Brands Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	5.8	18.4	N/A	N/A	14.2
MSCI World Index	7.5	19.1	N/A	N/A	18.1
Relative Performance	(1.6)	(0.6)	N/A	N/A	(3.3)

\*annualised, inception date 18/06/2012

### Purchases and Sales

During the quarter Morgan Stanley exited their position in Hermes and added to and reduced their positions in select Consumer Staples, Consumer Discretionary and Information Technology names on relative valuation grounds.

#### Top 3 Contributions to Return

Nestle	0.8%
Reckitt Benckiser	0.8%
Unilever	0.6%

#### Bottom 3 Contribution to Return

Microsoft	(0.5%)
Procter & Gamble	(0.2%)
Twenty First Century Fox	(0.1%)

### Top Ten Holdings

Company	Industry	% Weighting
Nestle	Food Products	9.6
British American Tobacco	Tobacco	9.2
Reckitt Benckiser	Household Products	7.0
Unilever	Food Products	7.0
Microsoft	Software	6.2
Accenture	IT Services	4.8
Time Warner	Media	4.7
Procter & Gamble	Household Products	4.6
Diageo	Beverages	4.5
Visa	IT Services	4.1

### Hymans Robertson View

There was no significant business news from Morgan Stanley over the period.

**Lincolnshire Pension Fund  
Passive Bonds – Blackrock  
Quarterly Report March 2015**

**Investment Process**

Blackrock manage a passive bond mandate for the Pension Fund. Their portfolio is made up of three pooled funds; an index-linked bond fund, a corporate bond fund and an overseas bond fund. All three funds are designed to match the return of their relevant benchmarks. The manager uses two methods to manage index-tracking funds; full replication and stratified sampling.

Full replication involves holding each of an index's constituent bonds in exactly the same proportion as the index. This method is used where the number of constituents in an index is relatively low and liquidity is above a certain level.

Stratified sampling is the method used when full replication is not possible or appropriate. This approach subdivides the benchmark index according to various risk characteristics, such as currency/country, maturity, credit rating, sector of issuer etc. Each subset of bonds is then sampled to select bonds for inclusion within the pooled fund.

The table below shows the indexing method for each of the three pooled funds in which the Fund invests.

<b>Pooled Fund</b>	<b>Indexing Method</b>
Aquila Life Corporate Bond All Stocks Index Fund	Sampled
Aquila Life Over 5 Years UK Index-Linked Gilt Index Fund	Full Replication
Aquila Life Overseas Bond Index Fund	Sampled

**Portfolio Valuation at 31st March 2015**

<b>Portfolio</b>	<b>31.12.14 £</b>	<b>31.03.15 £</b>
Corporate Bond All Stocks Index Fund	54,038,112	58,331,925
Over 5 Years UK Index-Linked Gilt Index Fund	33,150,635	34,465,335
Overseas Bond Index Fund	21,402,944	23,380,074
<b>Total</b>	<b>108,591,691</b>	<b>116,177,344</b>

**Performance**

Over all periods the portfolio has slightly outperformed the benchmark.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock	3.3	14.5	7.3	n/a	7.8
Composite Benchmark	3.2	14.2	7.2	n/a	7.7
Relative Performance	0.1	0.3	0.1	n/a	0.1

\*annualised since inception 28/07/10

### Hymans Robertson View

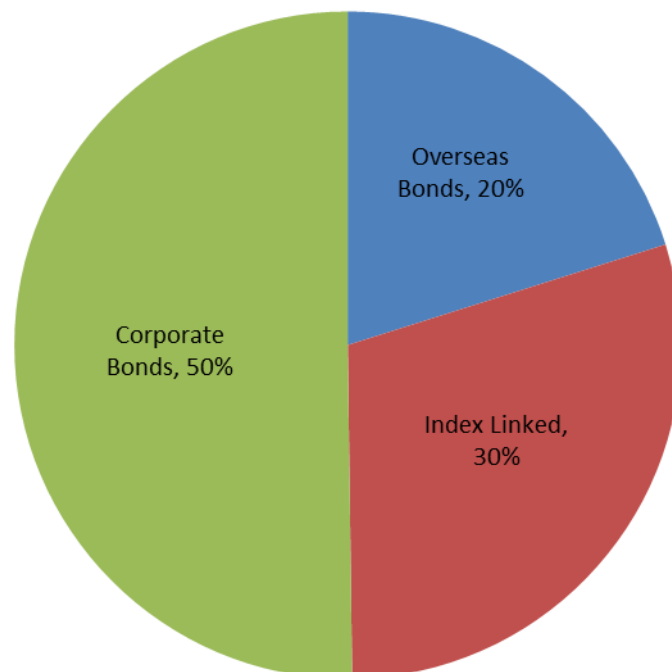
There were no significant developments within the Index Fixed Income team over the quarter; as such Hymans continue to rate Blackrock as one of their preferred passive fixed income managers.

### Allocation

The target allocation between the three funds is:

Aquila Life Corporate Bond All Stocks Index Fund	50%
Aquila Life Over 5 Years UK Index-Linked Gilt Index Fund	30%
Aquila Life Overseas Bond Index Fund	20%

The pie chart below shows the allocation as at 31<sup>st</sup> March 2015



**Lincolnshire Pension Fund  
Absolute Return Bonds – F&C  
Quarterly Report March 2015**

**Investment Process**

F&C manage an absolute return bond mandate for the Fund. The Pension Fund is invested in their multi-manager target return fund, with an investment objective to achieve a low level of return in excess of anticipated money market returns, within a multi-manager structure. The managers are selected to exploit various investment opportunities, including the money market, interest rate, equity, commodity, currency and credit markets. The manager has a target to beat the return of 3 month LIBOR +3%.

**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£97,880,872	£112,371,266

**Performance**

F&C produced a positive return of 1.4% during the quarter which was 0.7% above target. The positive return in the quarter was driven by recovering oil prices, which appeared to finally find their floor during January. Even before oil prices rose, dispersion returned to credit markets, which F&C would expect to benefit both Concerto's and Threadneedle's credit selection. Performance over longer periods continues to be behind the target.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
F&C	1.4	(1.3)	2.0	n/a	1.9
3 Month LIBOR + 3%	0.8	3.1	3.1	n/a	3.2
Relative Performance	0.7	(4.3)	(1.1)	n/a	(1.3)

\* annualised since inception date 19/07/2010

**Allocation**

The target return fund is currently split between three managers, listed below with their speciality investment areas:

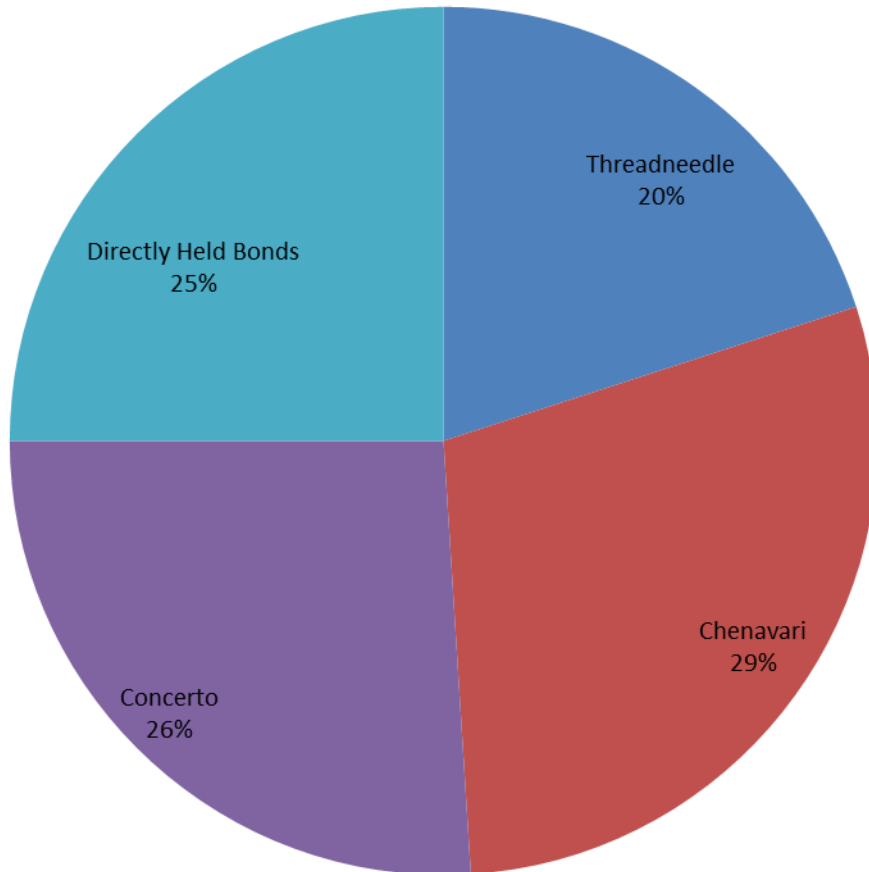
Threadneedle	Interest rates, currency
Chenavari	Credit
Concerto	Credit

**Hymans Robertson View**

Hyman's maintain their "retain" rating for F&C and feel the acquisition by BMO was positive and over the past year they have honoured their reputation as being a "hands off" owner. Hymans continue to believe BMO brings much needed stability to the ownership of the F&C business. Lincolnshire Pension Fund remains the largest investor in the Fund. However, under BMO ownership, the distribution reach

of the Fund has significantly increased and Hymans have been reassured that further investors into the Fund are being actively sought.

The pie chart below shows the allocation as at 31<sup>st</sup> March 2015



**Lincolnshire Pension Fund  
Alternative Investments – Morgan Stanley  
Quarterly Report March 2015**

**Investment Process**

Morgan Stanley manages a bespoke absolute return alternative investment mandate for the Fund. The portfolio is invested in alternatives only, with no exposure to traditional equities or bonds. Investments are made to complement our existing portfolio and in future will include our Private Equity portfolio. The manager has a target to beat the return of 3 Month LIBOR + 4%.

**Portfolio Valuation**

Value at 31.12.14	Value at 31.03.15
£155,911,580	£171,685,176

**Performance**

Morgan Stanley produced a positive return of 0.5% during the quarter but underperformed their target by 0.7%. Real assets were the primary detractor, particularly within commodities, however positive performance within the broad alpha portfolio and expanded credit generated offsetting gains. Tactical allocations were additive, while manager selection detracted. Morgan Stanley's decision to reduce exposure to commodities in favour of high yield was particularly beneficial. Manager selection, while strong in frontier equity, high yield and convertibles, was largely offset by hedge funds and global macro. Nevertheless, hedge funds were still the top absolute contributor, followed by high yield and senior loans. Commodities were once again the largest detractor, weighed down by a soaring USD and slowing growth around the world.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	0.5	1.0	4.6	n/a	5.0
3 Month LIBOR + 4%	1.2	4.7	4.7	n/a	4.8
Relative Performance	(0.7)	(3.5)	(0.1)	n/a	0.2

\* annualised since inception date 24/11/2010

**Allocation**

Morgan Stanley has split out investments into a bespoke portfolio of alternatives comprising five different asset allocations;

Alpha – These are pure return seeking products based on Manager skill. The Alpha investments include Hedge Funds, Global Tactical Asset Allocation (GTAA) and Active Currency.

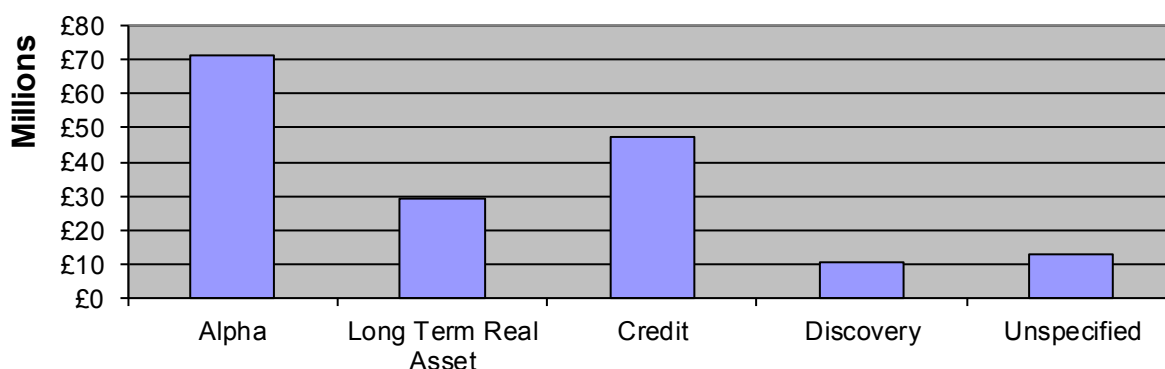
Long Term Real Asset – These are long term investments that seek to access illiquidity premium. Investments include Private Equity, Infrastructure, Real Estate, Commodities and Inflation – linked strategies.

Credit – These are the purchase of the lower rated bonds where higher default is more likely. Manager selection is important to ensure the correct bonds are purchased that will appreciate following rating upgrades and merger and acquisition activity. Credit opportunities include Emerging Market Debt, High Yield Bonds, Senior Loans and Convertibles.

Discovery – These are new opportunities of investments and can include Frontier Markets, Distressed Opportunities and Volatility.

Unspecified – These are cash balances held with Morgan Stanley.

**Allocation as at 31st March 2015**



## Portfolio Positioning

Given Morgan Stanley's view of near term weakness in economic fundamentals, they value alpha over beta and therefore restructured their hedge fund allocation during the quarter. They are moving their core exposure out of the diversified pooled fund of hedge funds into a more concentrated customised mandate unique to Lincolnshire that will seek to further enhance risk adjusted returns and better complement other parts of the overall portfolio. Morgan Stanley anticipate interest rates to be lower for longer and have reduced allocations to senior loans and inflation linked assets accordingly. During the quarter they also reduced their exposure to commodities given the continued relative strength of the USD and weakness in the energy sector.

## Hymans Robertson View

Hymans continue to rate Morgan Stanley a "5-preferred manager" for Diversified Alternatives.

## Risk Control

Portfolio volatility since inception is 3.87% within the guidelines specified by the mandate.

## Conclusion



Over the quarter the Fund has produced a positive return of 4.6% which is slightly behind the benchmark. Managers all produced a positive return in the quarter.

## **Consultation**

### **a) Policy Proofing Actions Required**

n/a

## **Background Papers**

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

This report was written by Nick Rouse, who can be contacted on 01522 553641 or [nick.rouse@lincolnshire.gov.uk](mailto:nick.rouse@lincolnshire.gov.uk).

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