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## Regulatory and Other Committee

<b>Open Report on behalf of Executive Director of Finance and Public Protection</b>
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Report to:	<b>Pensions Committee</b>
Date:	<b>08 October 2015</b>
Subject:	<b>Performance Measurement Annual Report</b>

**Summary:**

This report sets out the Pension Fund's longer term investment performance, for the period ending 31st March 2015.

**Recommendation(s):**

That the Committee note the report & consider the recommendation to revise the Fund performance target.

## Background

### 1 INTRODUCTION

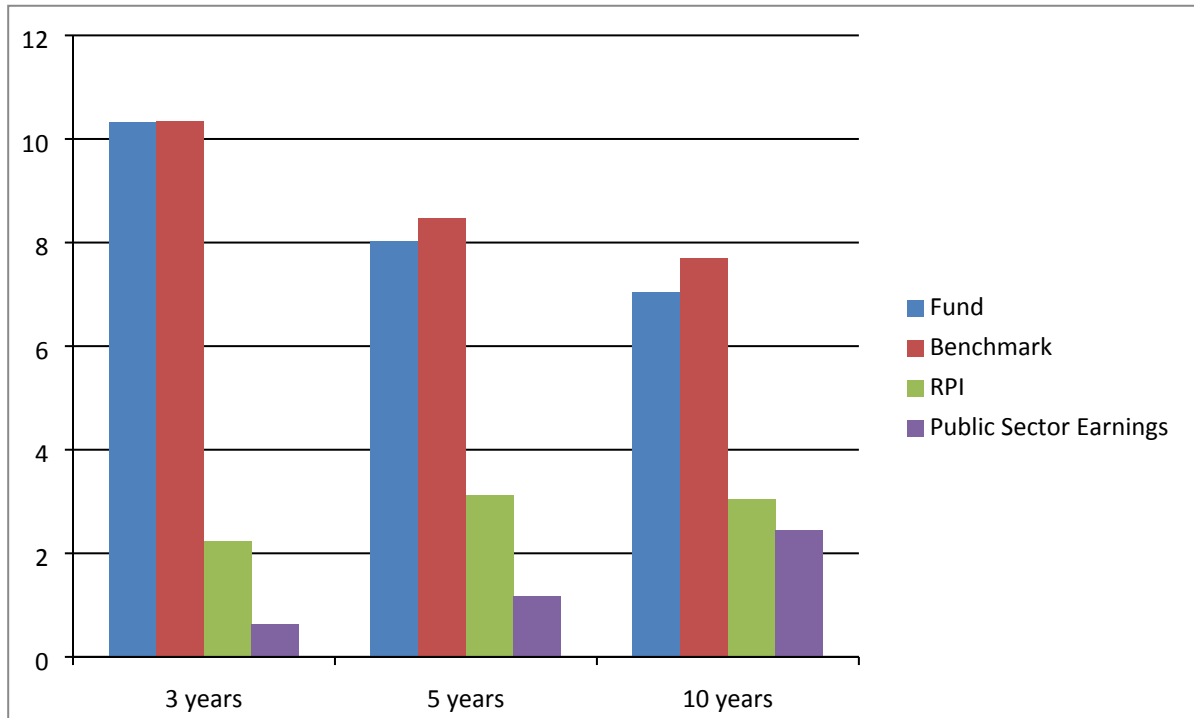
1.1 The Pension Fund uses two suppliers for the measurement of the Fund's performance. JPMorgan, the Fund's custodian, calculates the Fund's investment performance and compares it with the returns of the strategic asset allocation benchmark (i.e. the return achieved by the mix of assets as recommended by the Actuary). The WM Company compare the Fund's performance against the average Local Authority Pension Fund. The Fund's long term aim is to outperform the strategic benchmark by 1% per annum.

### 2 LONGER TERM PERFORMANCE FOR YEARS ENDED 31 MARCH 2015

2.1 The short term performance of the Fund and its managers is reported in the quarterly Investment Management report. This report will focus on the longer term performance of the Fund overall, compared to its strategic benchmark and the pay and price increases that impact the liabilities of the Fund. At the latest valuation, as at March 2013, the Actuary has calculated the employers contribution strategy based on an assumed annual return of 4.6% over the long term.

2.2 The graph and table below show longer term Fund and Benchmark performance, along with the increases in consumer prices and public sector earnings.

**INFLATION INCREASES AND INVESTMENT RETURNS FOR UP TO 10 YEARS ENDED 31/3/2015**



	3 years annualised %	5 years annualised %	10 years annualised %
Retail Prices Index increases	2.2	3.1	3.1
Public sector average Earnings increases	0.6	1.2	2.4
<b>LCC Fund performance</b>	<b>10.3</b>	<b>8.0</b>	<b>7.0</b>
<b>LCC Benchmark Performance</b>	<b>10.3</b>	<b>8.5</b>	<b>7.7</b>
<b>Relative Performance</b>	<b>0.0</b>	<b>(0.5)</b>	<b>(0.7)</b>

2.3 10 Year Returns

The Fund's performance over ten years, at 7%, is slightly behind the Fund's Benchmark return of 7.7%. This return is ahead of both inflation and average earnings over the last ten years, to which the scheme's liabilities are linked, which were 3.1% and 2.4% p.a. The Fund's performance reflects poor stock selection by the Fund's active asset managers over a number of years, as can be seen in the table at paragraph 3.4.

## 2.4 5 Year Returns

Five year returns of 8% per annum are ahead of both price and pay inflation. The Fund's actual performance is behind the strategic Benchmark return of 8.5%. This reflects the underperforming active managers over the period.

## 2.5 3 Year Returns

Three year returns, at 10.3%, are ahead of both inflation and average earnings, and match the strategic benchmark return.

## 3 ATTRIBUTION ANALYSIS

3.1 The attribution of the return over any period can be split between asset allocation and stock selection.

3.2 The asset allocation contribution reflects the extent to which decisions to deviate from the strategic benchmark, e.g. to be overweight cash and underweight equities, added to or detracted from performance, compared to the benchmark.

3.3 The stock selection contribution reflects the extent to which managers have or have not exceeded their benchmark index.

3.4 The Fund's annual performance over the last ten years compared to the Benchmark is set out in the tables below. Generally, stock selection has detracted from overall performance. This supports research that shows that active management generally detracts from performance over time, and the difficulty in selecting active managers that perform well over the long term. This may also be due to the timing of the appointment and termination of fund managers, when they are generally appointed after a period of good performance, and terminated after a period of poor performance.

## Long Term Performance Analysis

Year ended March	Fund %	Benchmark %	Relative Performance %	Attributed to Asset allocation %	Attributed to Stock Selection %
<b>2006</b>	24.4	24.1	<b>0.3</b>	0.7	(0.4)
<b>2007</b>	6.9	6.5	<b>0.3</b>	0.4	(0.1)
<b>2008</b>	(4.4)	(3.3)	<b>(1.1)</b>	0.1	(1.2)
<b>2009</b>	(18.6)	(20.0)	<b>1.7</b>	2.1	(0.4)
<b>2010</b>	29.7	36.7	<b>(5.1)</b>	(3.1)	(2.1)
<b>2011</b>	7.9	7.8	<b>0.1</b>	0.1	0.0
<b>2012</b>	1.5	2.4	<b>(0.8)</b>	(0.2)	(0.6)
<b>2013</b>	12.6	11.3	<b>1.2</b>	0.12	1.04
<b>2014</b>	6.3	6.2	<b>0.1</b>	0.15	(0.08)
<b>2015</b>	12.3	12.4	<b>(0.1)</b>	(0.09)	(0.07)

#### 4 WM LOCAL AUTHORITY UNIVERSE

- 4.1 The WM Company (a wholly owned subsidiary of State Street) measures the performance of the Fund against the Local Authority Universe. The WM Local Authority (LA) Universe is an aggregation of 85 funds within the LGPS sector that are used for peer group comparisons.
- 4.2 The weighted average return for Local Authority Pension Funds in the WM Local Authority Universe over the year 2014/15 was 13.2%, slightly ahead of the Lincolnshire Fund return of 12.3%. The actual performance of the Fund ranked in the middle of the Local Authority funds, at the 68<sup>th</sup> percentile. Over the longer term, the Fund is in the 70<sup>th</sup> to 80<sup>th</sup> percentile.
- 4.3 The table below shows how the asset allocation for the Lincolnshire Fund compares with the average Local Authority Pension Fund in 2015 and 2014.

Asset Class	Lincolnshire	LA Average	
		2015	2014
Equities	60.0	62	63
Bonds	13.5	17	16
Property	11.5	8	8
Alternatives	15.0	10	10
Cash	0.0	3	3

- 4.4 Since the 1990's Funds have been using strategic benchmarks linked to their individual liability profiles, rather than a standard asset allocation. The asset allocation of the Fund was considered at the July 2014 meeting of this committee, and the high level growth/low risk asset allocations agreed.

- 4.5 Within the LA Universe, there has been an increase in bonds and a reduction in equities. Within equities, the move from UK to global equities has continued.

## **5 FUND PERFORMANCE TARGET**

- 5.1 As requested at the July meeting of this committee a review of the Fund's objective to meet the strategic benchmark by 1% per annum, over the long term has been carried out by Hymans Robertson.
- 5.2 The Fund's consultant, Hymans Robertson, and officers have given consideration to the objective and propose reducing the target to 0.75% outperformance.
- 5.3 Paul Potter will present Hymans Robertson's paper and explain the reasoning behind the reduction from 1% to 0.75%
- 5.4 The Committee is asked to approve the amendment to the objective of the Fund to outperform the strategic benchmark by 0.75%, over the long term.

## **Conclusion**

- 6.1 The Pension Fund's investment performance of 7% over the 10 year period ended 31<sup>st</sup> March 2015 was slightly behind the strategic benchmark of 7.7%. The Fund is seeking to outperform the Benchmark by 1% per annum over rolling three year periods. Annualised returns over three, five and ten year periods are ahead of inflation in pay and prices. At an absolute level, the ten year performance is comfortably ahead of the current actuarial assumption for return of around 4.6% per annum.
- 6.2 Looking at the individual years, there was a negative contribution from both asset allocation and stock selection in the year ended March 2015. In eight of the last ten years, stock selection has detracted from performance.
- 6.3 The recommendation is made to amend the outperformance objective of the Fund from 1% to 0.75% above the strategic benchmark.

## **Consultation**

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

n/a

## Appendices

These are listed below and attached at the back of the report	
Appendix A	Hymans Robertson - Fund Performance Target Review

## Background Papers

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

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