

Agenda Item 7



Regulatory and Other Committee

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

Report to:	Pensions Committee
Date:	07 January 2016
Subject:	Investment Management Report

Summary:

This report covers the management of the Lincolnshire Pension Fund assets, over the period from 1st July to 30th September 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 31st March 2013 to 30th September 2015, for the Fund.
- 1.2 As the graph below shows, the funding level at the latest formal valuation was 71.5%. As at 30th September 2015 the funding level has decreased to 66.4%.

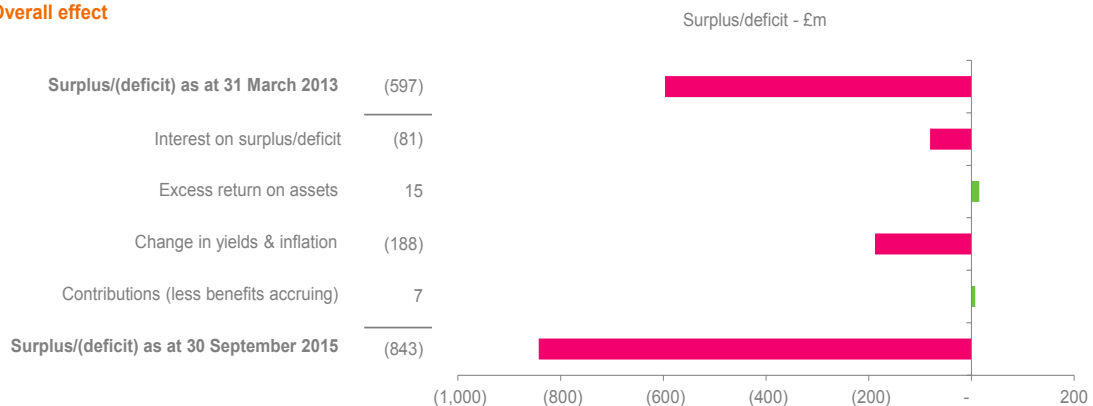
Change in funding level since last valuation



- 1.3 As shown below, the deficit in real money has increased from £597m to £843m between the period 31st March 2013 and 30th September 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 offset by a decrease in inflation.

What's happened since last valuation?

Overall effect



- 1.4 In the period since 30th June 2015, the funding level has decreased from 71% to 66.4% as a result of a further decrease in bond yields.

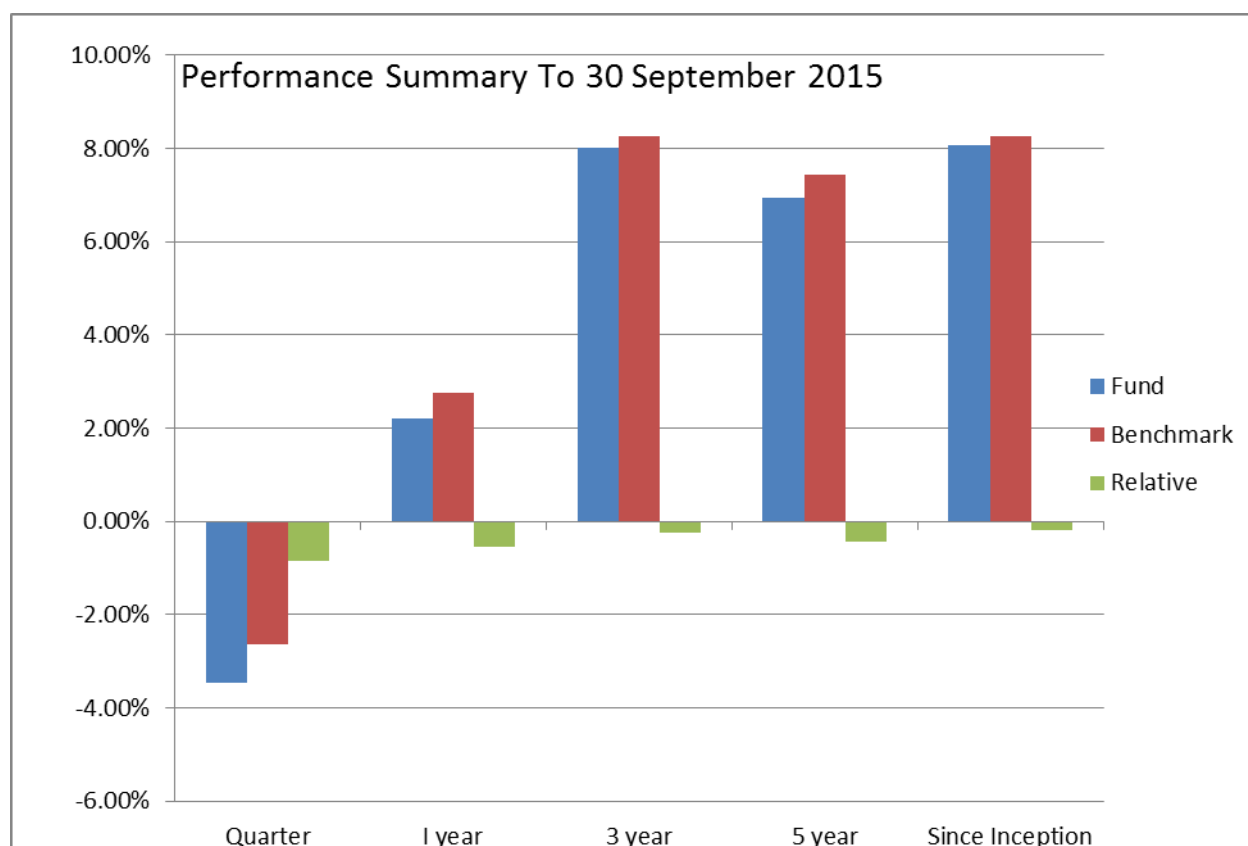
2. Fund Performance & Asset Allocation

2.1 The Fund decreased in value by £56.8m during the quarter from £1,714m to £1,657.2m, as the chart below shows. The Fund was overweight to cash and property and underweight equities and alternatives.

Asset Class	Q3 2015 £	Q2 2015 £	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	325.6	342.2	19.6	20.0	(0.4)
Global Equities	662.7	693.2	40.0	40.0	0.0
Alternatives	246.6	253.6	14.9	15.0	(0.1)
Property	197.1	197.4	11.9	11.5	0.4
Fixed Interest	223.4	222.4	13.5	13.5	0.0
Cash	1.8	5.2	0.1	0.0	0.1
Total	1,657.2	1,714.0	100.0	100.0	

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 0.75% per annum.

2.3 Over the quarter, the Fund produced a negative return of -3.46% and underperformed the benchmark which returned -2.64%. The Fund is behind the benchmark over all 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 three managers, Rreef Property Ventures Fund 3, Aviva Pooled Property Fund and Neptune as "on watch". Officers will monitor these managers closely and arrange meetings to discuss any potential issues

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 poor quarter for the Fund with all managers, except Blackrock, producing a negative absolute return. Over the quarter, six managers outperformed their benchmark, with Neptune, Morgan Stanley Alternatives and F&C all underperforming by 3.5%, 4.7% and 2.3%. Over the 12 month period only F&C, Morgan Stanley Alternatives and the In House Portfolio have failed to produce a positive absolute return. Against their target, the performance has been mixed with four managers failing to match their target.

	3 months ended 30/09/15			Previous 12 months			
Manager	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	Target p.a. %
Passive UK Equity In house	(6.1)	(6.1)	0.0	(3.7)	(3.4)	(0.3)	+/- 0.5
Invesco (Global Equities (ex UK))	(4.3)	(4.8)	0.6	2.3	1.5	0.9	+1.0
Threadneedle (Global Equities)	(4.2)	(5.9)	1.7	4.8	0.4	4.3	+2.0
Neptune (Global Equities)	(9.1)	(5.9)	(3.5)	2.9	0.4	2.5	+4.0
Schroder's (Global Equities)	(4.6)	(6.0)	1.5	3.5	(0.1)	3.6	+3.0
Morgan Stanley Global Brands	(0.6)	(4.9)	4.6	7.8	1.6	6.1	n/a
Blackrock (Fixed Interest)	2.4	2.4	0.0	6.8	6.5	0.3	Match Index
F&C (Fixed Interest)	(1.6)	0.8	(2.3)	(2.7)	3.1	(5.6)	3M LIBOR + 3%
Morgan Stanley (Alternative Investments)	(3.6)	1.2	(4.7)	(4.7)	4.7	(9.0)	3M LIBOR + 4%

**Lincolnshire Pension Fund
UK Equities – In House (Passive UK)
Quarterly Report September 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 30.06.15	Value at 30.09.15
£342,172,813	£325,659,115

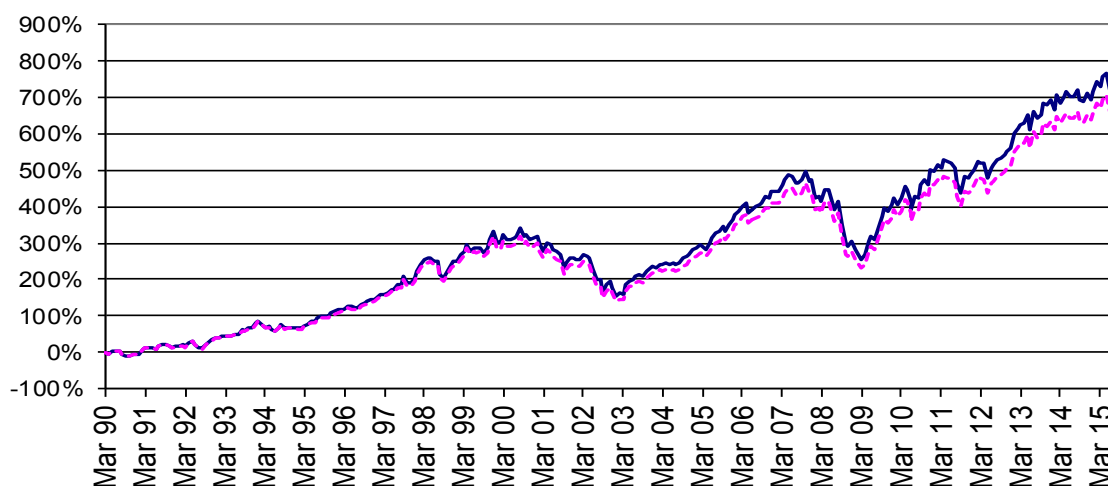
Performance

During the quarter the portfolio produced a negative return of 6.1% which matched the benchmark. The portfolio is slightly behind the benchmark over one and three year time periods but ahead over five years and since inception.

	Quarter %	1 Year %	3 Year*	5 Year*	Inception*
UK Equities – In House	(6.1)	(3.7)	6.4	6.5	8.1
MSCI UK IMI	(6.1)	(3.4)	6.5	6.4	7.8
Relative Performance	(0.0)	(0.3)	(0.1)	0.1	0.3

* annualised, inception date 01/10/1989

UK Equities In House Portfolio Performance Since Inception



Turnover

Holdings at 30.06.15	Holdings at 30.09.15	Turnover in Quarter %	Turnover in Previous Quarter %
255	263	1.6	0.0

Purchases and Sales

During the quarter the manager made several purchases and sales. New positions were taken in Workspace Group, Fevertree and Just Eat, whilst stock was added to RBS, Whitbread and BT. The manager sold out of XL Group, South32 Ltd and Colt Group as they exited the index.

Largest Overweights

Babcock	0.11%
Indivior	0.18%
Inmarsat	0.10%
Travis Perkins	0.10%
Hikma Pharmaceuticals	0.10%

Largest Underweights

Glencore	(0.10%)
HSBC	(0.09%)
Paysafe	(0.08%)
Diageo	(0.07%)
Astrazeneca	(0.07%)

* Measured against MSCI UK IMI

Top 10 Holdings

1	Royal Dutch Shell	£17,596,439	6	Vodafone Group	£9,818,654
2	HSBC Holdings	£17,188,305	7	Astrazeneca	£9,152,049
3	British American Tobacco	£11,952,355	8	Diageo	£7,807,711
4	GlaxoSmithkline	£11,151,728	9	Lloyds Banking Group	£7,623,997
5	BP	£10,669,643	10	Barclays	£7,312,032

Risk Control

The portfolio has a tracking error limit of 0.5%. At the end of September 2015 the tracking error was 0.26%.

Lincolnshire Pension Fund
Global Equities – Invesco (Global Ex UK Enhanced)
Quarterly Report September 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.

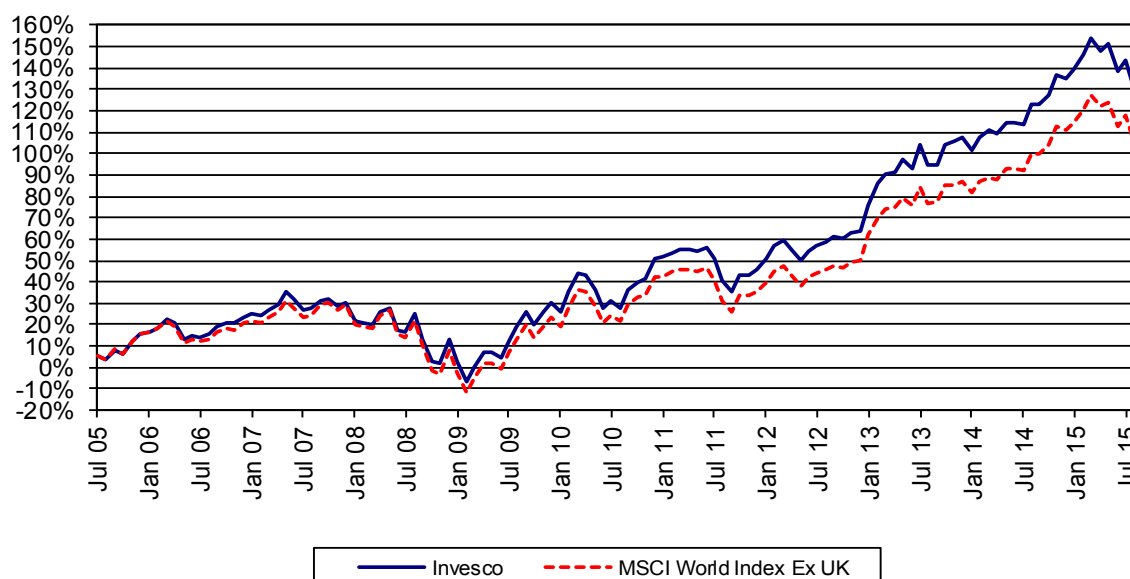
Portfolio Valuation

Value at 30.06.15	Value at 30.09.15
£344,469,542	£329,822,684

Performance

During the quarter Invesco's strategy outperformed its benchmark. Stock Selection had the largest positive impact on relative performance. Their momentum-related concepts Earnings Expectation and Management & Quality contributed positively to the development of the strategy. While the allocation in stocks with attractive scores in the Market Sentiment concept added to return, the intended overweights in the Value hurt performance.

Invesco Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	(4.3)	2.3	12.4	10.8	8.6
MSCI World ex UK	(4.8)	1.5	11.2	9.3	7.3
Relative Performance	0.6	0.9	1.1	1.4	1.2

* annualised, inception date 1st July 2005

Turnover

Holdings at 30.06.15	Holdings at 30.09.15	Turnover in Quarter %	Turnover in Previous Quarter %
438	457	10.1	11.4

Purchases and Sales

During the quarter Invesco made a number of stock adjustments to the portfolio as a result of their stock selection process. Invesco increased their positions in General Electric, Macquarie, Walt Disney and Apple. These were funded by selling out of Health Net, Allstate and Delhaize Group and decreased their positions in NTT and HP.

Largest Overweights

Intel	1.02%
Pfizer	0.96%
Apple	0.92%
JPMorgan Chase	0.86%
Citigroup	0.83%

Largest Underweights

Google	(0.66%)
Amazon	(0.56%)
Exxon Mobil	(0.55%)
Chevron	(0.52%)
Coca Cola	(0.42%)

* Measured against MSCI World ex UK (NDR)

Top 10 Holdings

1	Apple Inc	£10,323,621	6	Intel Corp	£4,973,106
2	JPMorgan Chase	£5,394,985	7	Citigroup Inc	£4,433,629
3	Pfizer Inc	£5,358,574	8	Johnson & Johnson	£4,171,723
4	Microsoft Corp	£5,295,599	9	Comcast Corp	£3,316,568
5	General Electric Co	£5,170,781	10	Cisco Systems	£3,090,975

Hymans Robertson View

There were no relevant business issues reported over the period.

Risk Control

The predicted tracking error of the portfolio slightly increased to 1.07% (actual target 1%).

**Lincolnshire Pension Fund
Global Equities – Neptune
Quarterly Report September 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.

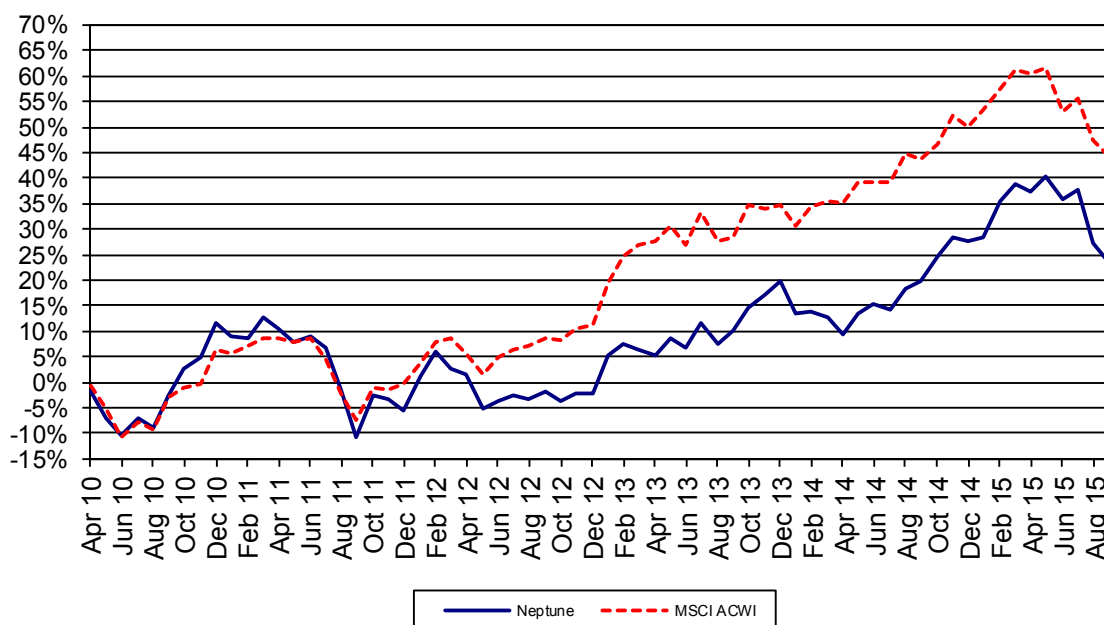
Portfolio Valuation

Value at 30.06.15	Value at 30.09.15
£89,662,366	£81,983,621

Performance

During the quarter Neptune produced a negative return of 9.1% and underperformed the benchmark by 3.5%. This was due to significant volatility in August, precipitated by renewed concerns over the possibility of a "hard landing" in China. This led to negative returns in emerging market indices, and China was the worst affected, falling nearly 20%. This had a knock on effect, particularly in Japan as global multinationals with exposure to China suffered.

Neptune Performance Since Inception



	Quarter %	1 Year %	3 Year %	5 Year %	Inception* %
Neptune	(9.1)	2.9	7.9	4.8	4.1
MSCI ACWI**	(5.9)	0.4	9.8	8.3	7.2
Relative Performance	(3.5)	2.5	(1.8)	(3.2)	(2.9)

* annualised, inception date 16/04/2010

Turnover

Holdings at 30.06.15	Holdings at 30.09.15	Turnover in Quarter %	Turnover in Previous Quarter %
55	53	9.0	5.9

Purchases and Sales

Neptune made a number of changes to the portfolio during this period, including buying two more Japanese companies, Keyence Corp, and make-up manufacturer, Shiseido Co Ltd, whilst shedding Japanese robot maker Fanuc. Neptune also sold a number of US stocks, including credit card provider American Express and healthy food supermarket, Whole Foods Market Inc.

Top 5 Contributions to Return

Google Inc	0.6%
Amazon.com	0.4%
Taisei Corp	0.4%
Kajima Corp	0.3%
Nike Inc	0.3%

Bottom 5 Contributions to Return

Komatsu Ltd	(0.5%)
Baidu.com	(0.5%)
Mitsubishi	(0.5%)
Dai-ichi Life Insurance	(0.5%)
NSK Ltd	(0.7%)

Top 10 Holdings

1	Google Inc	£3,489,918
2	Starbucks Corp	£3,000,891
3	Apple Inc	£2,912,164
4	CME Group Inc	£2,753,326
5	Mitsubishi Estate	£2,686,672

6	Mitsui Fudosan Co	£2,610,438
7	Sumitomo Realty	£2,609,363
8	Linkedin Corp	£2,509,193
9	Dai-ichi Life Ins Co	£2,398,712
10	Daiwa Securities	£2,326,523

Hymans Robertson View

There were no relevant business issues to report over the period but Hymans will reviewing their rating in fourth quarter following a further research meeting.

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 September 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.

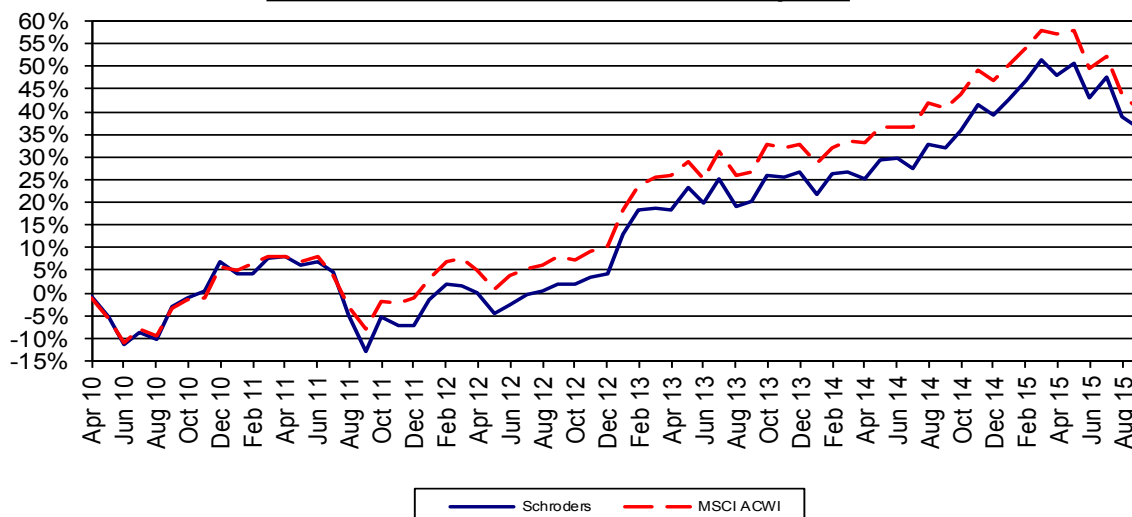
Portfolio Valuation

Value at 30.06.15	Value at 30.09.15
£85,441,059	£81,496,556

Performance

Schroders outperformed the benchmark over the period, driven by strong stock selection, particularly in the technology sector. Their holdings in healthcare and materials sector also added to relative return. The main detractor was stock selection in Japan. Over one and three years Schroders have outperformed the benchmark but underperformed over five years and since inception.

Schroders Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Schroders	(4.6)	3.5	10.3	7.1	6.1
MSCI ACWI (Net)	(6.0)	(0.1)	9.3	7.8	6.7
Relative Performance	1.5	3.6	0.9	(0.7)	(0.6)

*annualised since Inception April 16 2010

Turnover

Holdings at 30.06.15	Holdings at 30.09.15	Turnover in Quarter %	Turnover in Previous Quarter %
69	67	7.1	10.8

Purchases and Sales

During the quarter Schroders increased their exposure to the consumer sector with new purchases in TripAdvisor and Mondelez. Sales this quarter included stocks where they were concerned about the demand outlook in China such as auto companies manufacturer BorgWarner and Japanese housebuilder Sekisui House.

Top 5 Contributions to Return

Google Inc	0.6%
Safran	0.3%
Amazon.com	0.3%
Imperial Tobacco	0.3%
Reckitt Benckiser	0.3%

Bottom 5 Contributions to Return

SMC Group	(0.4%)
Cabot Oil & Gas	(0.3%)
Alibaba	(0.2%)
Tenet Healthcare	(0.2%)
Daikin Industries	(0.2%)

Top 10 Holdings

1	Google Inc	£2,512,320	6	Danaher Corp	£1,854,437
2	Citigroup Inc	£2,063,963	7	JPMorgan Chase & Co	£1,802,633
3	Pfizer Inc	£2,057,050	8	Comcast Corp	£1,779,204
4	Taiwan Semiconductor	£1,910,944	9	Cognizant Tech	£1,776,692
5	Reckitt Benckiser	£1,881,834	10	Nestle	£1,763,964

Hymans Robertson View

Hymans have reviewed Schroders during the quarter and sufficiently encouraged by the actions Alex Tedder has taken over the last 12 months to restore their "retain" rating.

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 September 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.

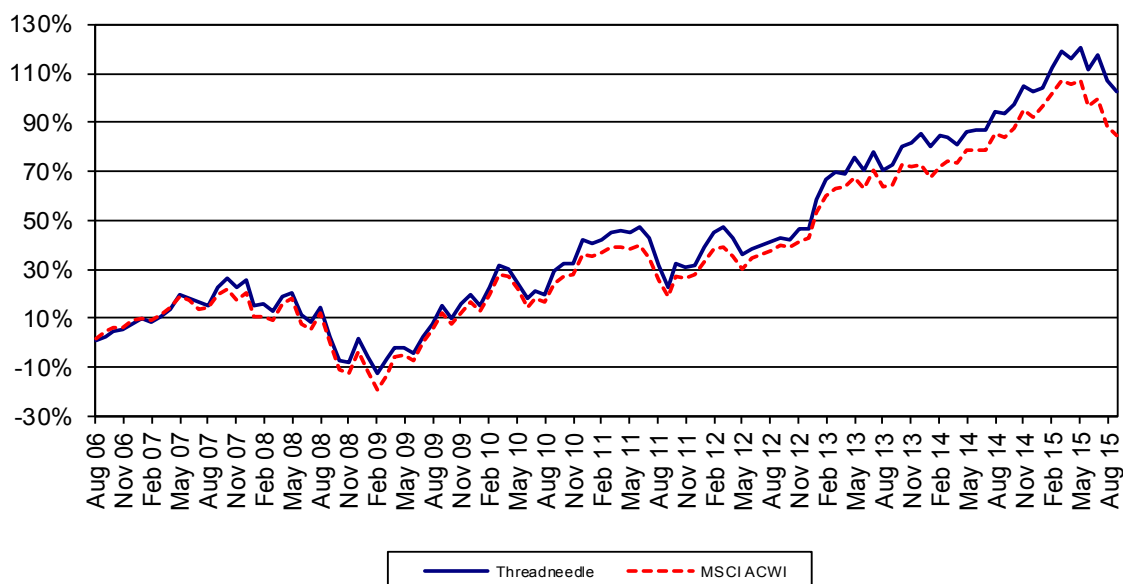
Portfolio Valuation

Value at 30.06.15	Value at 30.09.15
£88,102,935	£84,380,768

Performance

Threadneedle outperformed its benchmark in the quarter. Regional allocation added value as developed Asia, where they are underweight, underperformed. Over all periods Threadneedle are ahead of the benchmark and are ahead of their target over 1 and 3 years.

Threadneedle Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Threadneedle	(4.2)	4.8	12.3	9.4	8.5
MSCI ACWI	(5.9)	0.4	9.8	8.2	7.3
Relative Performance	1.7	4.3	2.3	1.0	1.1

* annualised, inception date 01/08/2006

Turnover

Holdings at 30.06.15	Holdings at 30.09.15	Turnover in Quarter %	Turnover in Previous Quarter %
83	85	8.3	9.3

Purchases and Sales

Threadneedle opened a position in Royal Dutch Shell to reduce their underweight position in energy. They also initiated a new position in medical equipment company Zimmer Biomet. These were funded by selling their holding in investment bank Nomura during the quarter.

Top 5 Contributions to Return

Google Inc	0.3%
Nike Inc	0.3%
Amazon.com	0.2%
Sabre Corp	0.2%
Markit Ltd	0.2%

Bottom 5 Contributions to Return

Methanex Corp	(0.6%)
WESCO International	(0.4%)
Gilead Sciences	(0.4%)
Mazda	(0.3%)
Spirit Airlines	(0.3%)

Top 10 Holdings

1	Google Inc	£2,252,889	6	Priceline Group	£1,706,277
2	Gilead Sciences	£2,228,722	7	Aon PLC	£1,690,974
3	Facebook Inc	£2,208,090	8	Amphenol Corp	£1,607,717
4	UBS AG	£1,920,021	9	Mastercard Inc	£1,600,715
5	Comcast Corp	£1,867,746	10	Apple Inc	£1,593,099

Hymans Robertson View

There was no relevant business issues reported over the period.

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 September 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.

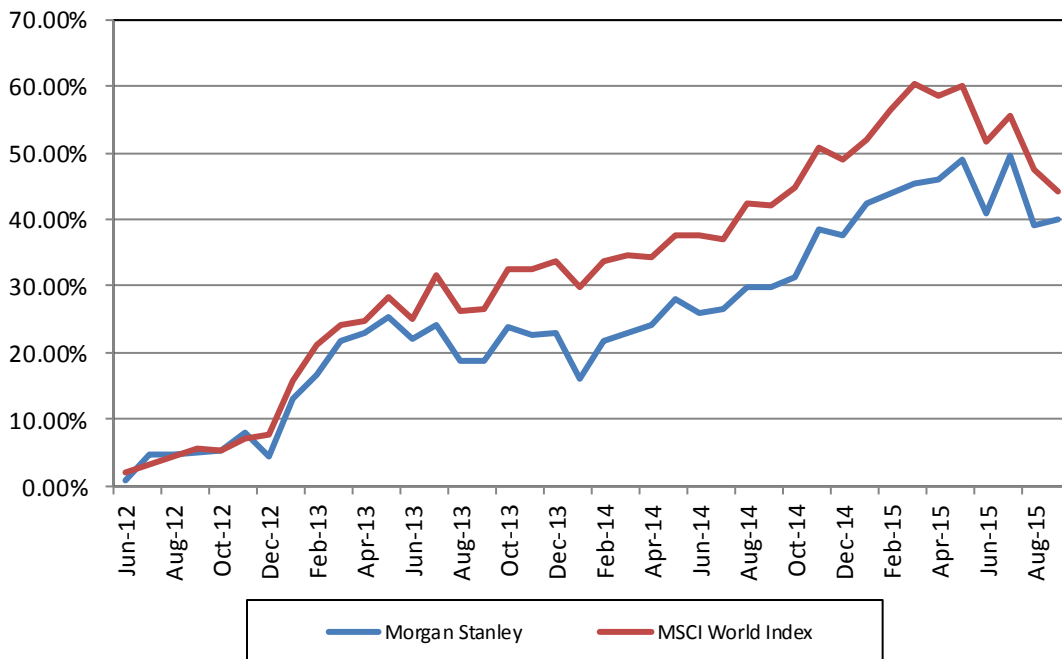
Portfolio Valuation

Value at 30.06.15	Value at 30.09.15
£85,570,518	£85,073,555

Performance

During the quarter Morgan Stanley Global Brands returned -0.58% outperforming its benchmark by 4.6%, which returned -4.94%. The outperformance for the quarter was mainly due to large Consumer Staples positions which were up in the tough market. The worst performers came from US Media, on the back of the August scare about rising cord-cutting.

Morgan Stanley Global Brands Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	(0.6)	7.8	10.0	N/A	12.6
MSCI World Index	(4.9)	1.6	10.9	N/A	13.8
Relative Performance	4.6	6.1	(0.8)	N/A	(1.1)

*annualised, inception date 18/06/2012

Purchases and Sales

During the quarter Morgan Stanley added to some of their Media names and reduced some of their positions in Consumer Staples, Pharma and Luxury Goods on relative valuation grounds.

Top 3 Contributions to Return

British American Tobacco	1.1%
Nestle	1.0%
Reckitt Benckiser	1.0%

Bottom 3 Contribution to Return

Time Warner	(0.6%)
21 st Century Fox	(0.3%)
Japan Tobacco	(0.2%)

Top Ten Holdings

Company	Industry	% Weighting
Nestle	Food Products	9.5
British American Tobacco	Tobacco	9.0
Reckitt Benckiser	Household Products	7.4
Microsoft	Software	6.8
Unilever	Personal Products	6.7
Accenture	IT Services	4.8
Altria Group	Tobacco	4.8
Mondelez	Food Products	4.6
Time Warner	Media	4.1
Visa	IT Services	4.0

Hymans Robertson View

In July, Morgan Stanley has announced two new experienced hires for the International Equity team that manages the Global Brands / Franchise strategy. Yiwon Li left the team at the end of March 2015. The manager has since made two new hires, Nic Sochovsky (ex-Credit Suisse) and Richard Perrott (ex-Autonomous Research / Brenberg Bank). We do not know these individuals from their previous employment but we are encouraged to see the team being strengthened.

**Lincolnshire Pension Fund
Passive Bonds – Blackrock
Quarterly Report September 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.

Pooled Fund	Indexing Method
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 30th September 2015

Portfolio	30.06.15 £	30.09.15 £
Corporate Bond All Stocks Index Fund	56,102,690	56,649,063
Over 5 Years UK Index-Linked Gilt Index Fund	33,332,957	34,111,942
Overseas Bond Index Fund	21,632,164	22,970,482
Total	111,067,811	113,731,487

Performance

Over all periods the portfolio has slightly outperformed the benchmark.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock	2.4	6.8	5.3	6.0	7.2
Composite Benchmark	2.4	6.5	5.2	6.0	7.2
Relative Performance	0.0	0.3	0.1	0.0	0.1

*annualised since inception 28/07/10

Hymans Robertson View

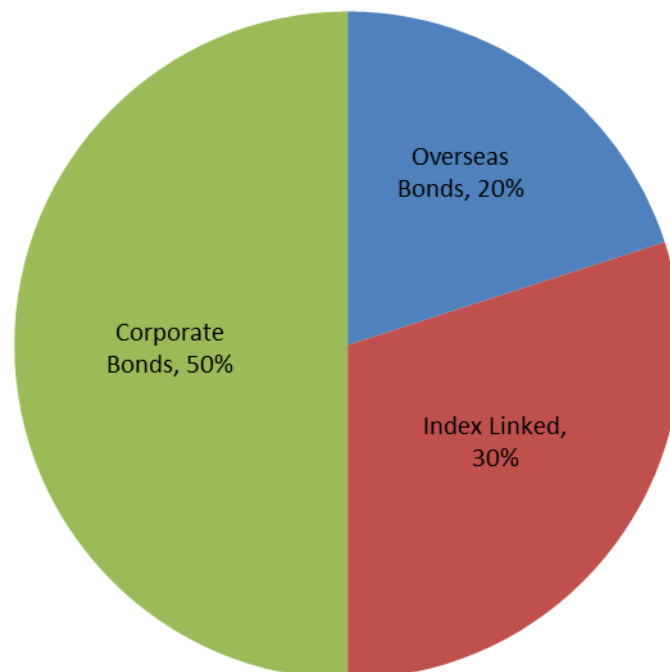
There were no significant developments within the Index Fixed Income team over the quarter; as such Hymans continue to rate Blackrock as one of their preferred passive fixed income managers.

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 30th September 2015



**Lincolnshire Pension Fund
Absolute Return Bonds – F&C
Quarterly Report September 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 30.06.15	Value at 30.09.15
£111,368,676	£109,625,436

Performance

F&C produced a negative return of 1.6% during the quarter which was 2.3% below target. The most important contributor to F&C's return this quarter was the negative return from Chenavari, which was down 4.3% over the quarter, but they think this is likely to recover quickly. F&C have retained the relatively high exposure to short dated bonds in the portfolio, which has proven to be the right decision so far.

Over the mid-term, they are becoming nervous regarding government bond performance for the first time in many years and are waiting to see the reaction of the bond markets when the Fed finally start to increase rates and are hopeful that this will allow them to re-enter some rates and currency strategies in 2016.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
F&C	(1.6)	(2.7)	0.5	1.2	1.4
3 Month LIBOR + 3%	0.8	3.1	3.1	3.2	3.6
Relative Performance	(2.3)	(5.6)	(2.5)	(2.0)	(2.1)

* annualised since inception date 19/07/2010

Allocation

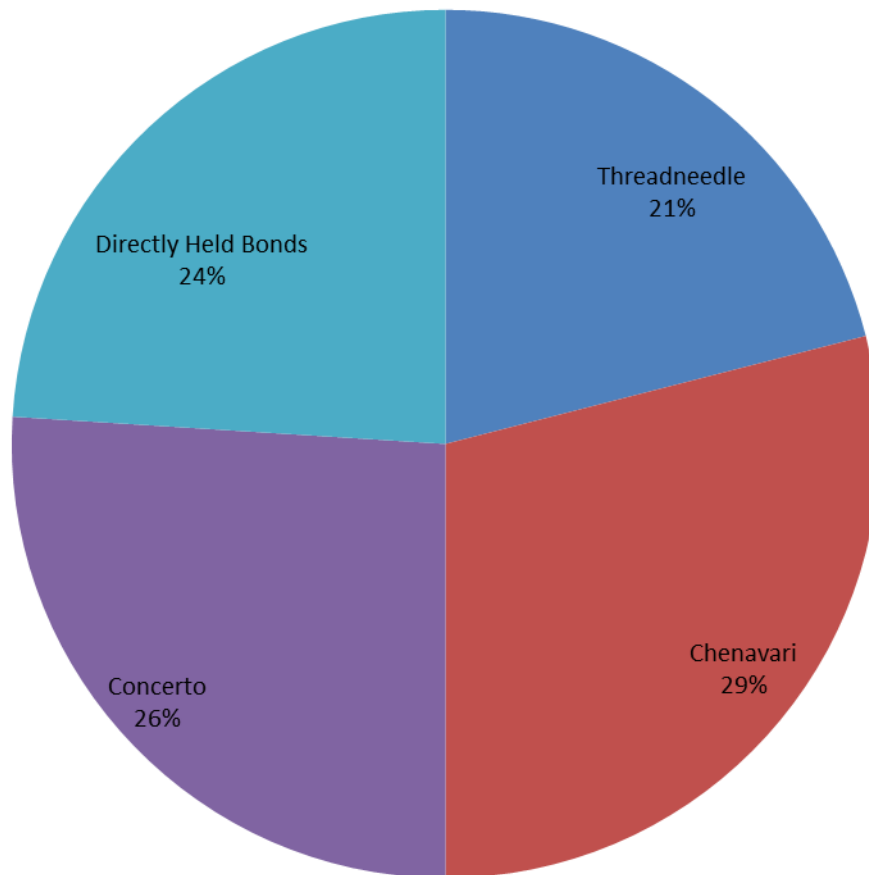
The target return fund is currently split between three managers, listed below with their speciality investment areas:

Threadneedle	Interest rates, currency
Chenavari	Credit
Concerto	Credit

Hymans Robertson View

Performance in 2015 has been disappointing given the absolute return benchmark. The Fund continues to be managed by Ben Fox and he is looking at adding other managers to the strategy and is currently undertaking the necessary due diligence.

The pie chart below shows the allocation as at 30th September 2015



**Lincolnshire Pension Fund
Alternative Investments – Morgan Stanley
Quarterly Report September 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 30.06.15	Value at 30.09.15
£178,878,880	£179,384,509

Performance

The portfolio returned -3.74% during the third quarter, as gains from real assets and catastrophe risk were insufficient to offset losses in credit and hedge funds. With the exception of EM debt, high yield and global macro, manager selection was positive in all asset classes. Tactical decisions were mixed. The decision to reduce the allocation to high yield over the quarter and increase their public real estate exposure in September was beneficial to performance. In contrast, their energy tilt in high yield dragged on returns.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	(3.6)	(4.7)	1.9	n/a	3.7
3 Month LIBOR + 4%	1.2	4.7	4.7	n/a	5.0
Relative Performance	(4.7)	(9.0)	(2.6)	n/a	(1.3)

* 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.

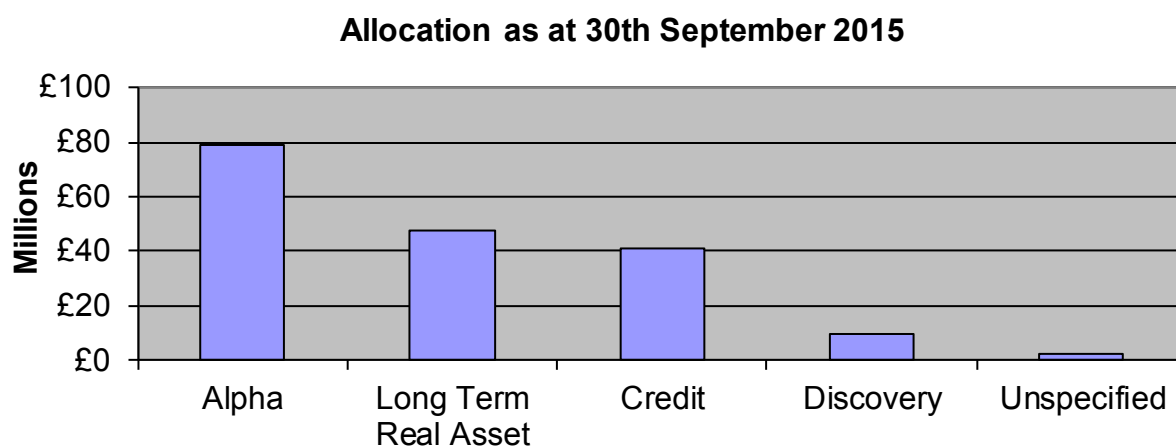
Long Term Real Asset – These are long term investments that seek to access illiquidity premium. Investments include Private Equity, Infrastructure, Real Estate, Commodities and Inflation – linked strategies.

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.



Portfolio Positioning

Given the uptick in volatility in both equity and credit markets and potential Fed rate increase, Morgan Stanley remain focused on alpha-oriented strategies (hedge funds) at the expense of credit strategies and commodities. This quarter, they continued to modestly add to the hedge fund portfolio while reducing their macro allocation. They also increased their exposure to catastrophe risk, reflecting their continued positive view on the asset class. They remain underweight credit given the imminent U.S. interest rate hike, feared slowdown in growth and decline in oil prices. In addition, they are cautious on EM debt given the China slowdown. Over the quarter they modestly decreased credit through reductions in high yield and EM debt. Within real assets, they are progressively making commitments to private infrastructure. On the liquid side, they have a preference for listed private equity over listed infrastructure, since the latter is more exposed to interest rate sensitivity. The portfolio held a significant tactical underweight to real estate securities heading into the third quarter in acknowledgement of its interest rate sensitivity, but the allocation was increased to a neutral weight at the end of August to reflect improving valuations. Lastly, they remain conservatively positioned on commodities as certain sectors are vulnerable to oversupply and a stronger USD.

Hymans Robertson View

Hymans feel the recent performance has been disappointing and will be undertaking a review of the manager and their rating in the fourth quarter of 2015.

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 negative return of -3.64% which is behind the benchmark.

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.

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