

Regulatory and Other Committee

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

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

Summary:

This report covers the management of the Lincolnshire Pension Fund assets, over the period from 1st October to 31st December 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

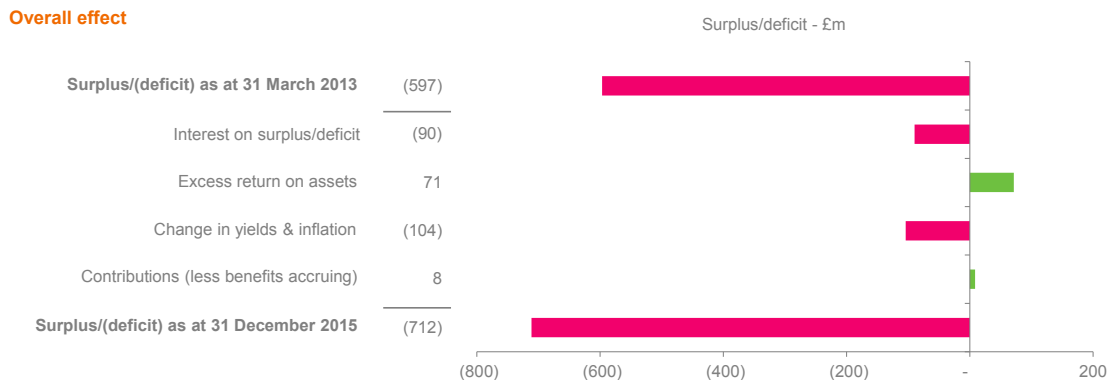
- 1.1 The funding update is provided to illustrate the estimated development of the funding position from 31st March 2013 to 31st December 2015, for the Fund.
- 1.2 As the graph below shows, the funding level at the latest formal valuation was 71.5%. As at 31st December 2015 the funding level has decreased to 71%.

Change in funding level since last valuation



1.3 As shown below, the deficit in real money has increased from £597m to £712m between the period 31st March 2013 and 31st December 2015. This is due to strong assets returns which have been offset by falling real bond yields which has increased the value of liabilities.

1.4 What's happened since last valuation?



1.5 In the period since 30th September 2015, the funding level has increased from 66.4% to 71%. This is due to yields having risen slightly which has placed a lower value on the liabilities. Combined with positive asset returns, this has resulted in a higher funding level and lower deficit amount at 31st December 2015.

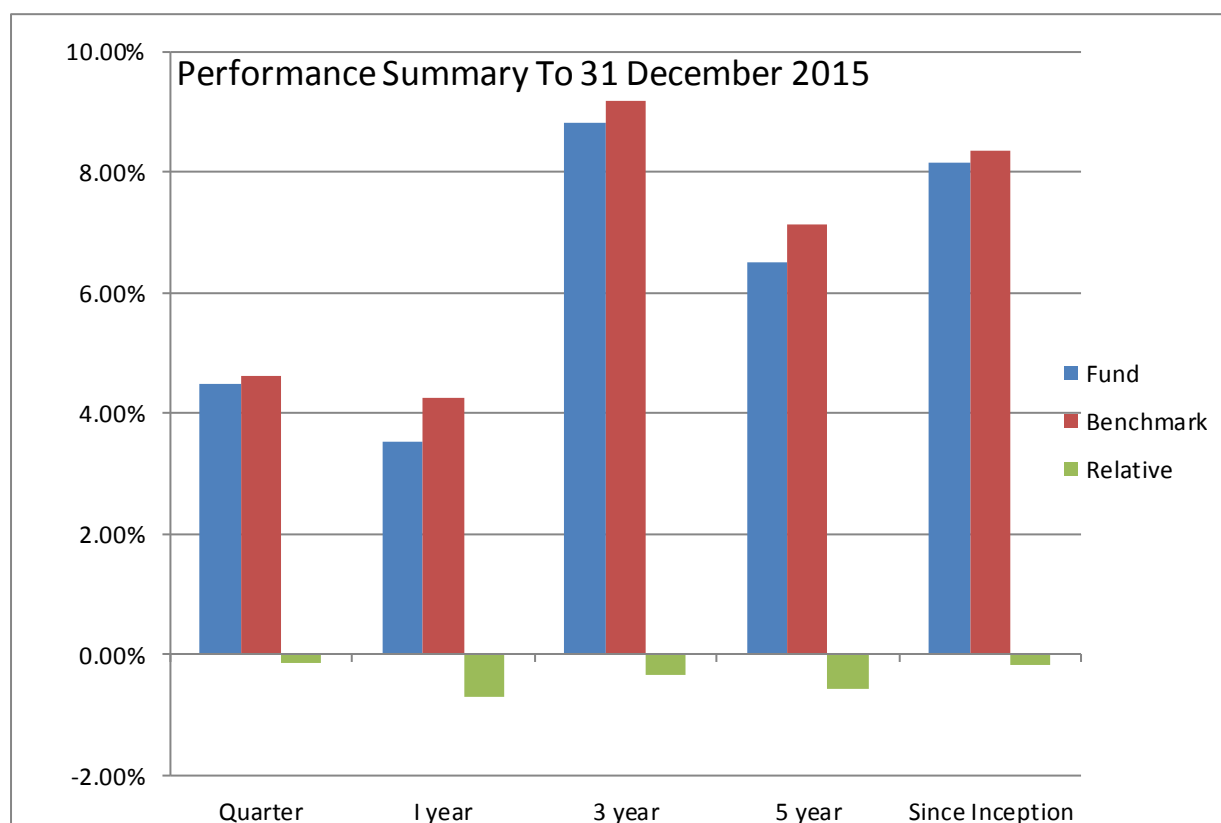
2. Fund Performance & Asset Allocation

2.1 The Fund increased in value by £75.4m during the quarter from £1,657.2m to £1,732.6m, as the chart below shows. The Fund was overweight to Cash and Global Equities and underweight UK Equities, Alternatives, Property and Fixed Interest.

Asset Class	Q4 2015 £	Q3 2015 £	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	337.5	325.6	19.5	20.0	(0.5)
Global Equities	721.8	662.7	41.7	40.0	1.7
Alternatives	247.1	246.6	14.3	15.0	(0.7)
Property	198.2	197.1	11.4	11.5	(0.1)
Fixed Interest	223.6	223.4	12.9	13.5	(0.6)
Cash	4.4	1.8	0.2	0.0	0.2
Total	1,732.6	1,657.2	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 positive return of 4.49% and underperformed the benchmark which returned -0.13%. 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 during the quarter there was one rating change with F&C going from "retain" to "on watch". Sixteen managers remained rated as retain and four managers, Reef Property Ventures Fund 3, Aviva Pooled Property Fund, Neptune and F&C 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 good quarter for the Fund with all managers, except Blackrock and Morgan Stanley Alternatives producing a positive absolute return. Over the quarter, only three managers outperformed their benchmark, Threadneedle, Schroder's and Morgan Stanley Global Brands. 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, Schroder's and Morgan Stanley Global Brands have performed well whilst F&C and Morgan Stanley Alternatives continue to disappoint.

	3 months ended 31/12/15			Previous 12 months			
Manager	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	Target p.a. %
Passive UK Equity In house	3.7	3.8	(0.1)	(0.2)	0	(0.2)	+/- 0.5
Invesco (Global Equities (ex UK))	8.7	8.8	(0.1)	5.6	4.7	1.0	+1.0
Threadneedle (Global Equities)	10.6	8.0	2.4	10.4	3.8	6.4	+2.0
Neptune (Global Equities)	6.5	8.1	(1.4)	2.8	3.8	(1.0)	+4.0
Schroder's (Global Equities)	8.5	7.9	0.5	6.3	3.3	2.9	+3.0
Morgan Stanley Global Brands	10.1	8.4	1.5	12.0	4.9	6.8	n/a
Blackrock (Fixed Interest)	(0.5)	(0.5)	0.0	0.7	0.5	0.2	Match Index
F&C (Fixed Interest)	0.7	0.8	(0.1)	(0.4)	3.1	(3.4)	3M LIBOR + 3%
Morgan Stanley (Alternative Investments)	(0.2)	1.1	(1.3)	(3.9)	4.7	(8.2)	3M LIBOR + 4%

**Lincolnshire Pension Fund
UK Equities – In House (Passive UK)
Quarterly Report December 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 30.09.15	Value at 31.12.15
£325,659,115	£337,523,109

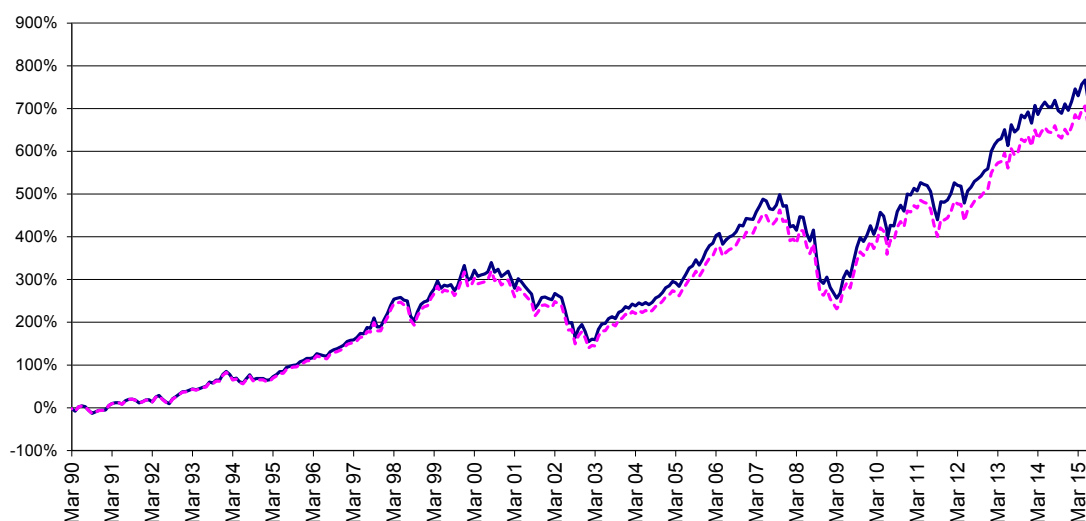
Performance

During the quarter the portfolio produced a positive return of 3.7% which was 0.1% below 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	3.7	(0.2)	6.4	5.8	8.1
MSCI UK IMI	3.8	0.0	6.5	5.7	7.8
Relative Performance	(0.1)	(0.2)	(0.1)	0.1	0.3

* annualised, inception date 01/10/1989

UK Equities In House Portfolio Performance Since Inception



Turnover

Holdings at 30.09.15	Holdings at 31.12.15	Turnover in Quarter %	Turnover in Previous Quarter %
263	274	0.5	1.6

Purchases and Sales

During the quarter the manager made several purchases. These included new positions in Optimal Payments and London Metric Property and an increase to the holdings of Glencore and HSBC.

Largest Overweights

Babcock	0.12%
Inmarsat	0.11%
Greene King	0.11%
Rangold Res	0.10%
Travis Perkins	0.10%

Largest Underweights

Auto Trader	(0.18%)
Abcam	(0.06%)
BWIN Party Digit	(0.05%)
Aviva	(0.05%)
Shire	(0.05%)

* Measured against MSCI UK IMI

Top 10 Holdings

1	HSBC	£18,561,551	6	Vodafone	£10,583,138
2	Royal Dutch Shell	£17,324,938	7	Astrazeneca	£10,328,992
3	British American Tobacco	£12,372,312	8	Diageo	£8,265,936
4	GlaxoSmithKline	£12,094,824	9	Lloyds Banking	£7,411,994
5	BP	£11,456,898	10	BT Group	£7,293,562

Risk Control

The portfolio has a tracking error limit of 0.5%. At the end of December 2015 the tracking error was 0.20%.

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

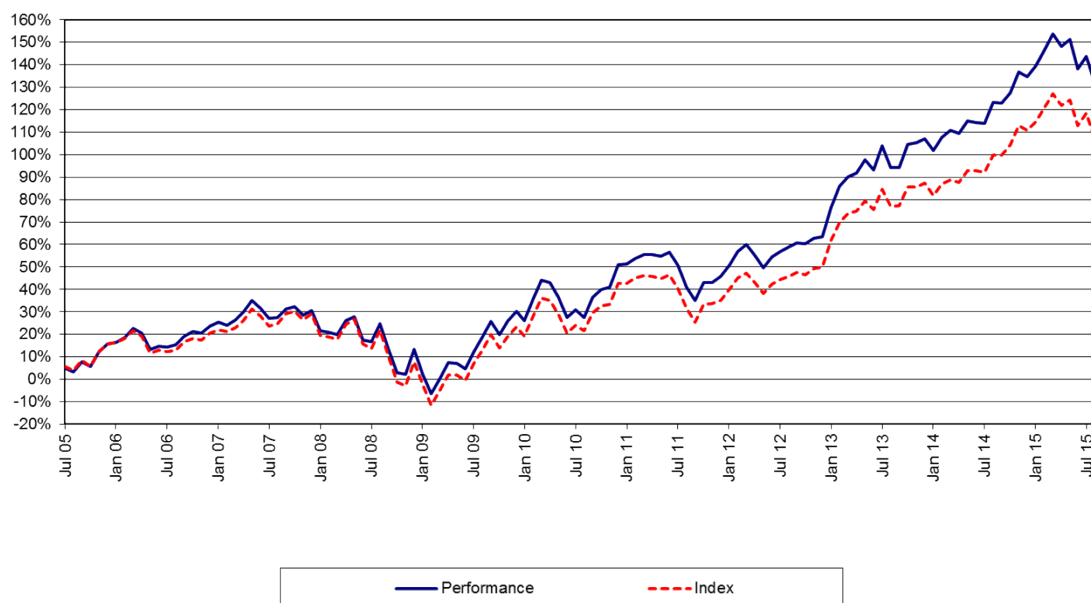
Portfolio Valuation

Value at 30.09.15	Value at 31.12.15
£329,822,684	£358,425,059

Performance

During the quarter Invesco's strategy underperformed its benchmark. Stock Selection had a slightly negative impact on relative performance, as the contribution from their overweighted assets was negative. Contributions from Countries and Currencies, were positive with the overweight position to New Zealand and an underweight position in Canada helping performance.

Invesco Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	8.7	5.6	14.9	10.4	9.0
MSCI World ex UK	8.8	4.7	13.7	9.1	7.8
Relative Performance	(0.1)	0.9	1.0	1.2	1.1

* annualised, inception date 1st July 2005

Turnover

Holdings at 30.09.15	Holdings at 31.12.15	Turnover in Quarter %	Turnover in Previous Quarter %
457	471	8.9	10.1

Purchases and Sales

During the quarter, Invesco made a number of stock adjustments to the portfolio. They 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 decreasing positions in NTT and HP.

Largest Overweights

Intel	1.03%
JP Morgan Chase	1.01%
Citigroup	0.94%
Apple	0.90%
General Electric	0.85%

Largest Underweights

Alphabet	(0.79%)
Chevron	(0.57%)
Exxon Mobil	(0.55%)
Coca-Cola	(0.43%)
Bristol-Myers Squibb	(0.38%)

* Measured against MSCI World ex UK (NDR)

Top 10 Holdings

1	Apple Inc	£10,308,548	6	Citigroup	£5,175,351
2	General Electric	£6,553,281	7	Johnson & Johnson	£5,134,848
3	JP Morgan Chase	£6,485,987	8	Comcast	£4,409,786
4	Microsoft	£6,000,594	9	Cisco Systems	£3,288,062
5	Intel	£5,584,612	10	Bank of America	£3,242,907

Hymans Robertson View

There were no relevant business issues reported over the period.

Risk Control

The predicted tracking error of the portfolio slightly decreased to 1.06% (actual target 1%).

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

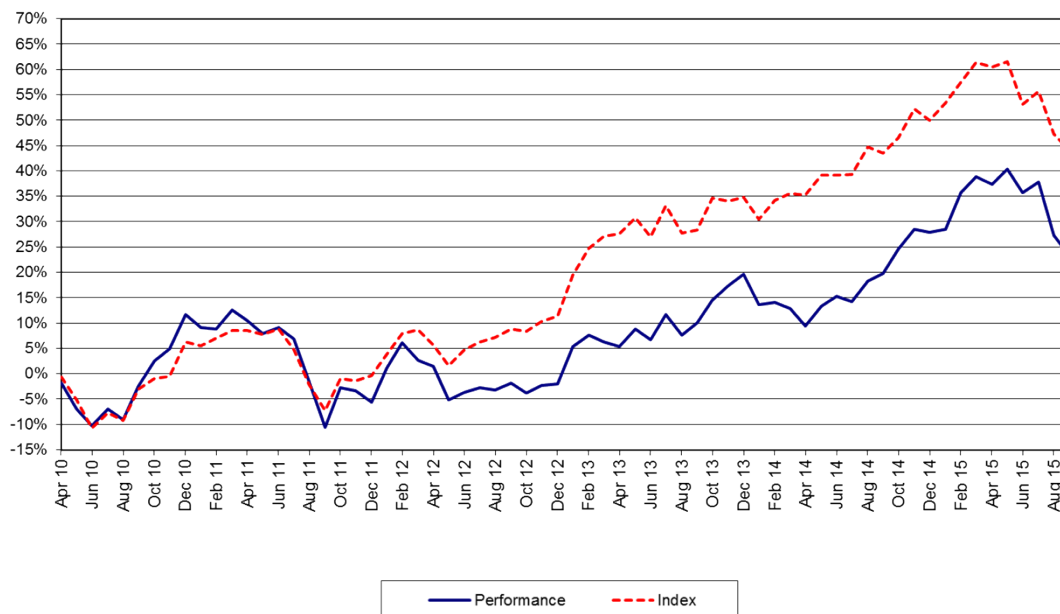
Portfolio Valuation

Value at 30.09.15	Value at 31.12.15
£81,983,621	£87,864,070

Performance

During the quarter Neptune produced a positive return of 6.5% and underperformed the benchmark by 1.4%. The Fund's exposure to world class Japanese multinationals contributed to outperformance as the stocks rebounded in the fourth quarter. However the absence of further quantitative easing continued to be felt, which led to yen strength and financials underperformance. The best performers in the Fund were once again Neptune's US technology and consumer holdings, with companies such as Amazon, LinkedIn and Home Depot enjoying another strong quarter. Neptune maintain their belief that the low oil price will continue to provide a boost to US consumer spending, whilst in the technology space they have maintained their structural overweight, as companies such as Amazon continue to grow their market share.

Neptune Performance Since Inception



	Quarter %	1 Year %	3 Year %	5 Year %	Inception* %
Neptune	6.5	3.6	10.3	3.3	5.3
MSCI ACWI**	8.1	3.8	11.8	7.9	8.0
Relative Performance	(1.4)	(0.2)	(1.6)	(4.3)	(2.7)

* annualised, inception date 16/04/2010

Turnover

Holdings at 30.09.15	Holdings at 31.12.15	Turnover in Quarter %	Turnover in Previous Quarter %
53	52	11.2	9.0

Purchases and Sales

Neptune continued to add to consumer exposure in Japan at the expense of some industrial stocks where they took profits. They also reduced their exposure to India, selling ICCI and Larsen & Toubro. They also added Under Armour to increase US domestic millennial consumption exposure.

Top 5 Contributions to Return

Alphabet	1.2%
Amazon.com	0.9%
Keyence	0.7%
Linkedin	0.6%
Baidu.com	0.6%

Bottom 5 Contributions to Return

Under Armour	(0.3%)
Nintendo	(0.3%)
Hain Celestial	(0.3%)
Isetan Mitsukoshi	(0.2%)
Sumitomo Realty & Dev	(0.2%)

Top 10 Holdings

1	Alphabet	£4,380,771	6	Mitsubishi Estate	£2,845,979
2	Starbucks	£3,257,752	7	Amazon	£2,843,023
3	CME Group	£3,170,839	8	Tencent Holdings	£2,668,313
4	Linkedin	£3,054,210	9	Keyence	£2,647,956
5	Apple	£2,855,553	10	Dai-ichi Life Insurance	£2,639,834

Hymans Robertson View

Hymans rating on Neptune Global Equity is currently at '3 - On Watch'. They were encouraged by the initiatives taken in 2015 by Neptune to improve its investment process. They would expect Robin Geffen's top down view to continue to dominate though they note that his ('correct') overweight call on Japan was undermined at the stock selection level in 2015.

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 December 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.

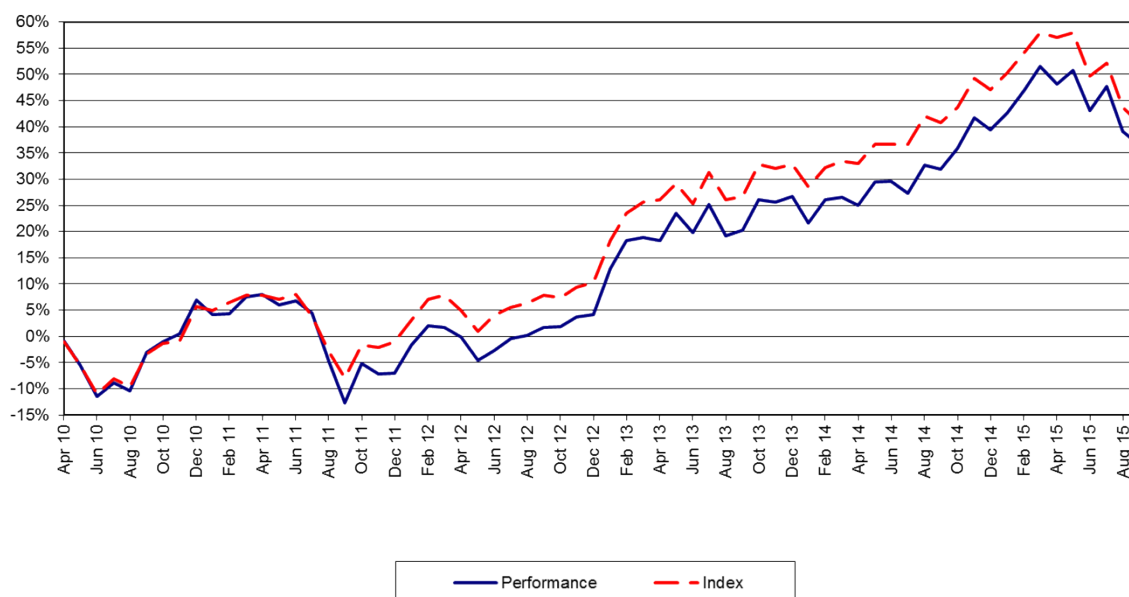
Portfolio Valuation

Value at 30.09.15	Value at 31.12.15
£81,496,556	£88,510,859

Performance

Schroders outperformed the benchmark over the period, driven by strong regional stock selection. They gained the most from their holdings in North America, Japan and the emerging markets. Offsetting this to some extent though, were their holdings in consumer staples, energy and financials.

Schroders Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Schroders	8.5	6.3	12.5	6.8	7.1
MSCI ACWI (Net)	7.9	3.3	11.3	7.5	7.5
Relative Performance	0.5	2.9	1.1	(0.7)	(0.4)

*annualised since Inception April 16 2010

Turnover

Holdings at 30.09.15	Holdings at 31.12.15	Turnover in Quarter %	Turnover in Previous Quarter %
67	69	9.8	7.1

Purchases and Sales

During the quarter Schroders purchased the Japanese industrial stock, Keyence and Japanese mobile operator KDDI. The sold their position in Japanese air-conditioning firm Daikin to fund these purchases.

Top 5 Contributions to Return

Google	0.4%
Amazon	0.4%
Daikin Industries	0.3%
Alibaba Group	0.3%
Smc Corp	0.2%

Bottom 5 Contributions to Return

Bbva	(0.3%)
Kasikornbank	(0.3%)
Cabot Oil & Gas	(0.2%)
Safran	(0.2%)
Microsoft	(0.2%)

Top 10 Holdings

1	Alphabet	£3,153,628
2	Amazon.com	£2,213,890
3	Citigroup	£2,213,112
4	TWN Semicont	£2,173,953
5	Pfizer	£1,973,048

6	Reckitt Benckiser	£1,971,729
7	Amgen	£1,917,332
8	Apple	£1,915,291
9	Visa	£1,873,428
10	Danaher	£1,855,032

Hymans Robertson View

There were 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 – Threadneedle Quarterly Report December 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.

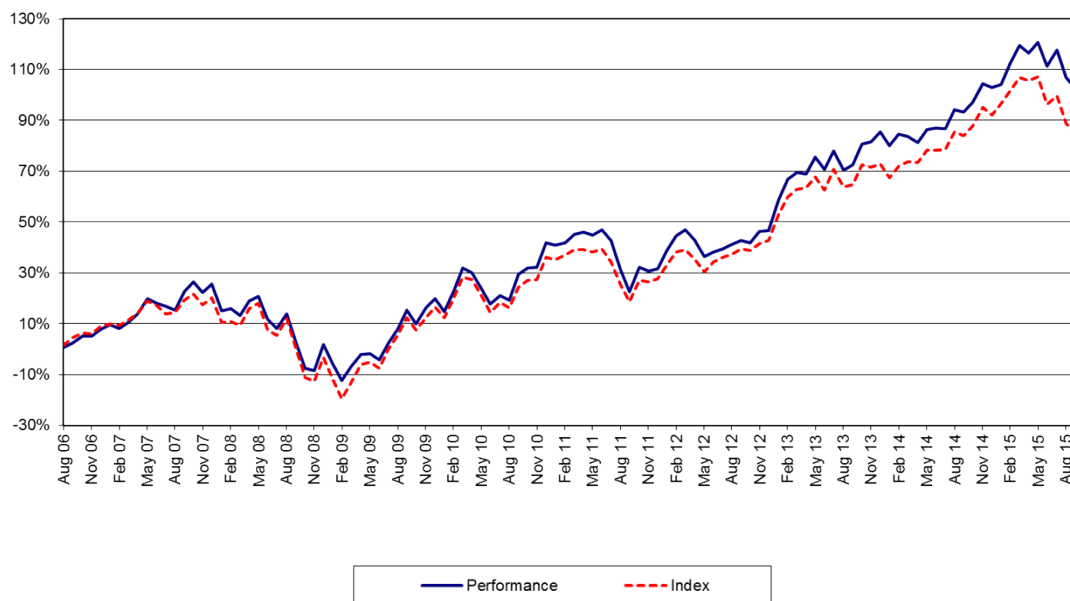
Portfolio Valuation

Value at 30.09.15	Value at 31.12.15
£84,380,768	£93,347,789

Performance

Threadneedle outperformed its benchmark in the quarter. Regional allocation detracted, as developed Asia and Japan, where they are underweight, both outperformed. Threadneedle's overweight in technology and underweight in energy were especially helpful to performance, as were their selections in technology and healthcare.

Threadneedle Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Threadneedle	10.6	10.4	14.6	9.0	8.3
MSCI ACWI	8.1	3.8	11.9	8.0	7.5
Relative Performance	2.4	6.4	2.5	1.0	0.8

* annualised, inception date 01/08/2006

Turnover

Holdings at 30.09.15	Holdings at 31.12.15	Turnover in Quarter %	Turnover in Previous Quarter %
85	88	2.7	8.3

Purchases and Sales

Threadneedle opened positions in China's Ping An Insurance, Nintendo and NXP Semiconductors. These were funded by exiting positions in Disney and Liberty Global.

Top 5 Contributions to Return

Alphabet	0.66%
Facebook	0.51%
Amazon.com	0.45%
PT Bank Rakyat	0.41%
Vertex Pharmaceuticals	0.38%

Bottom 5 Contributions to Return

Spirit Airlines	(0.14%)
Nintendo	(0.12%)
Union Pacific	(0.09%)
Wolseley	(0.05%)
American Express	(0.04%)

Top 10 Holdings

1	Alphabet	£2,927,973	6	Comcast	£1,905,663
2	Priceline	£2,365,193	7	Aon	£1,808,853
3	Gilead Sciences	£2,363,859	8	Continental	£1,784,572
4	Facebook	£2,253,962	9	Mastercard	£1,779,126
5	UBS Group	£2,088,772	10	JP Morgan Chase	£1,756,323

Hymans Robertson View

In December 2015 the FCA fined Threadneedle £6m for failing to put in place adequate controls on its dealing desk. This relates back to a situation in 2011 when a Threadneedle employee attempted a fraudulent trade. This was picked up and reported to the FSA (at the time) and the employee dismissed. The FCA subsequently ruled the firm's dealing controls were not sufficiently rigorous and subsequent remedial changes had not been fully implemented, hence the fine. The FCA is now fully satisfied with Threadneedle's dealing controls and, while the incident does not reflect well on the manager, its systems did work, no clients lost out and, in Hyman's judgement, this does not warrant a revision to their current ratings.

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 December 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.

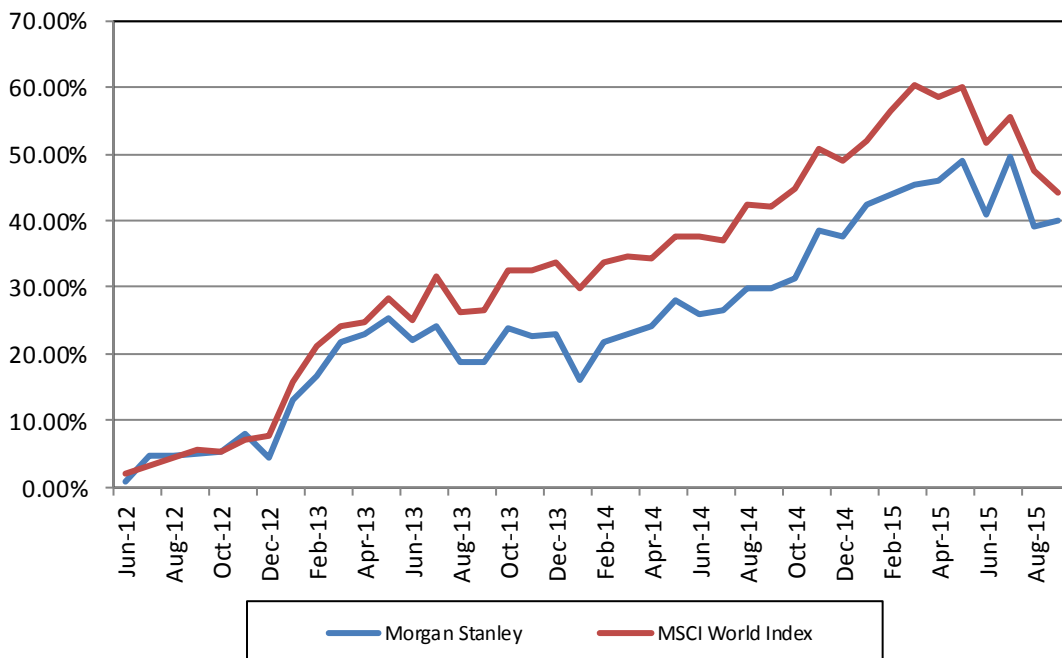
Portfolio Valuation

Value at 30.09.15	Value at 31.12.15
£85,073,555	£93,666,116

Performance

During the quarter Morgan Stanley Global Brands returned 10.1% outperforming its benchmark by 1.5%, which returned 8.42%. The outperformance for the quarter was mainly due to stock selection in Information Technology while their zero weights in Energy, Utilities and Materials and the underweight in Financials also contributed.

Morgan Stanley Global Brands Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	10.1	12.0	13.8	N/A	12.8
MSCI World Index	8.4	4.9	13.3	N/A	13.3
Relative Performance	1.5	6.8	0.5	N/A	(0.4)

*annualised, inception date 18/06/2012

Purchases and Sales

During the quarter Morgan Stanley retreated from areas where they are worried about the business, these included P&G and Mead Johnson. They made two purchases, in high quality companies, L'Oreal and Reynolds.

Top 3 Contributions to Return

Microsoft	2.07%
Unilever	0.66%
Visa	0.58%

Bottom 3 Contribution to Return

Sanofi	(0.16%)
L'Oreal	(0.10%)
Time Warner	(0.09%)

Top Ten Holdings

Company	Industry	% Weighting
Microsoft	Software	8.7
Nestle	Food Products	8.0
British American Tobacco	Tobacco	7.5
Reckitt Benckiser	Household Products	7.2
Unilever	Personal Products	5.8
Altria	Tobacco	4.9
Reynolds American	Tobacco	4.8
Mondelez	Food Products	4.7
Accenture	IT Services	4.6
Visa	IT Services	4.2

Hymans Robertson View

There were no relevant business issues reported over the period.

**Lincolnshire Pension Fund
Passive Bonds – Blackrock
Quarterly Report December 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 31st December 2015

Portfolio	30.09.15 £	31.12.15 £
Corporate Bond All Stocks Index Fund	56,649,063	56,878,545
Over 5 Years UK Index-Linked Gilt Index Fund	34,111,942	32,987,164
Overseas Bond Index Fund	22,970,482	23,384,837
Cash (residual)		10
Total	113,731,487	113,250,556

Performance

Over all periods the portfolio has slightly outperformed the benchmark.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock	(0.5)	0.7	4.4	6.2	6.5
Composite Benchmark	(0.5)	0.5	4.3	6.1	6.4
Relative Performance	0.0	0.2	0.1	0.0	0.1

*annualised since inception 28/07/10

Hymans Robertson View

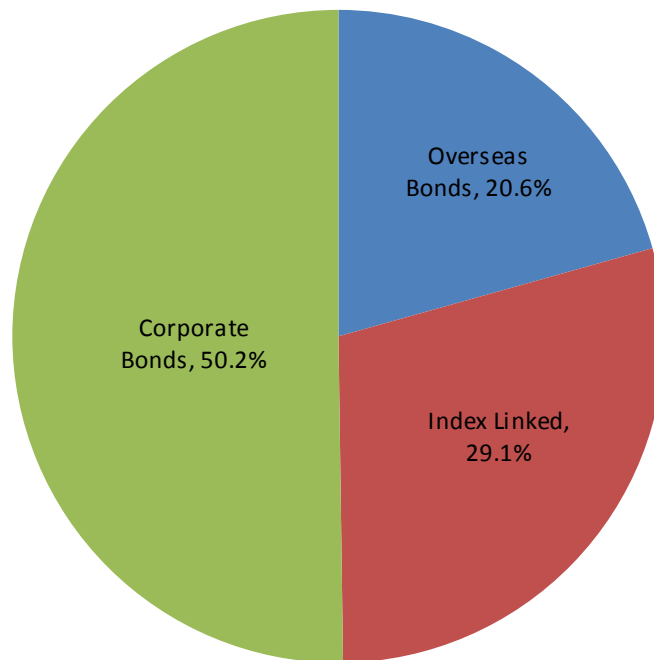
There were no significant developments within the Index Fixed Income team over the quarter; as such Hymans continue to rate Blackrock as one of their preferred passive fixed income managers.

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 31st December 2015.



**Lincolnshire Pension Fund
Absolute Return Bonds – F&C
Quarterly Report December 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 30.09.15	Value at 31.12.15
£109,625,436	£110,375,120

Performance

F&C produced a positive return of 0.7% during the quarter which was 0.2% below target. In the quarter, Chenavari came back strongly as they had hoped at the end of September. Concerto were down, as was the US high yield market and Columbia Threadneedle were flat.

Over 12 months, Comcerto were the main contributor to the negative performance, and there was no strong positive contributor to offset this..

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
F&C	0.7	(0.4)	(0.1)	1.2	1.3
3 Month LIBOR + 3%	0.9	2.7	2.9	3.1	3.1
Relative Performance	(0.2)	(3.0)	(2.9)	(1.9)	(1.8)

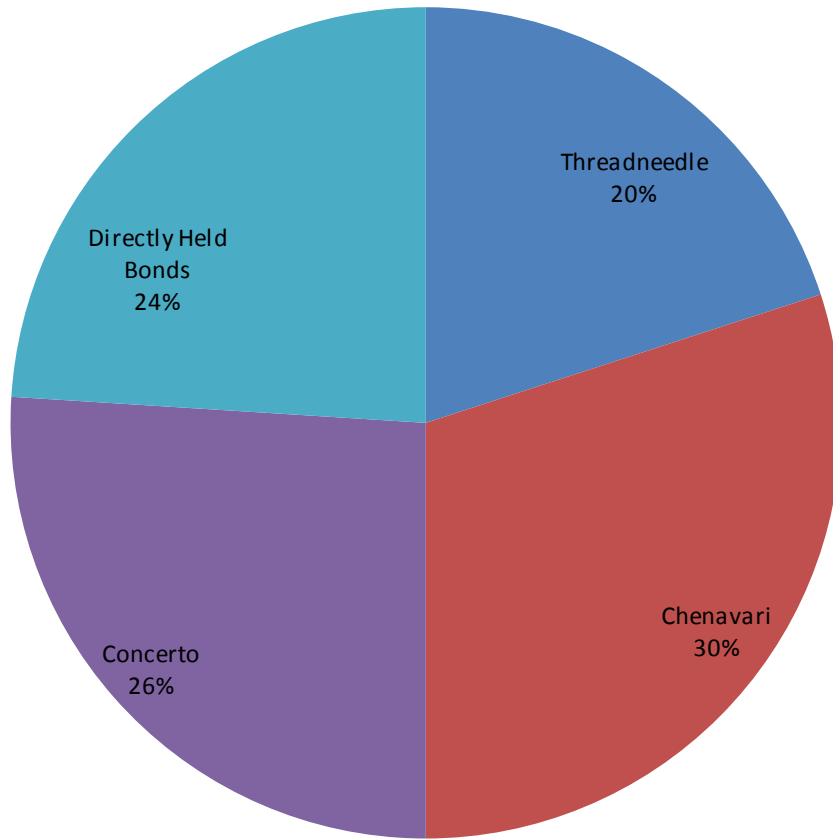
* annualised since inception date 19/07/2010

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

The pie chart below shows the allocation as at 31st December 2015



Hymans Robertson View

Although many absolute return bond managers struggled in 2015, the disappointing returns from F&C have gone on for much longer. Hymans will be discussing the options for this mandate with the Committee in May and they have changed their rating to "on watch".

**Lincolnshire Pension Fund
Alternative Investments – Morgan Stanley
Quarterly Report December 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 30.09.15	Value at 31.12.15
£179,384,509	£183,444,113

Performance

The portfolio returned -0.23% during the fourth quarter. The largest detractors to absolute performance were high yield bonds and commodities, while real estate was the primary contributor. Positive relative returns from tactical decisions were partly offset by manager selection. Within manager selection, senior loans, infrastructure and REIT's outperformed while hedge funds and more focused global asset allocation managers lagged.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	(0.2)	(3.9)	1.0	N/A	3.3
3 Month LIBOR + 4%	(1.2)	4.7	4.7	N/A	4.7
Relative Performance	(1.3)	(8.2)	(3.5)	N/A	(1.4)

* 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.

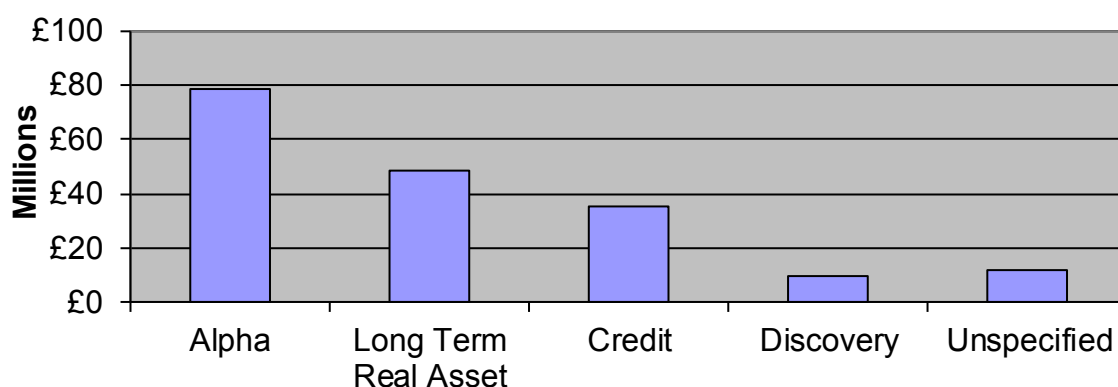
Credit – These are the purchase of the lower rated bonds where higher default is more likely. Manager selection is important to ensure the correct bonds are purchased that will appreciate following rating upgrades and merger and acquisition

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 December 2015



Portfolio Positioning

In recent months, equity and fixed income market volatility, driven by the potential Fed interest rate hike and global growth concerns spurred by the China slowdown, whipsawed markets and dampened beta-driven rallies. In this environment alpha oriented strategies are relatively more attractive. As such, Morgan Stanley continue to favour hedge funds and continued to add to the hedge fund portfolio over the quarter. They remain underweight credit due to liquidity concerns, low interest rates globally and expectations of Fed interest rate hikes. Over the quarter they made reductions to EM debt through redemptions in two investments as their alpha generation has lagged given the difficult growth environment in EM. Within real assets, they continue to progressively make 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 allocation to listed private equity reflects their positive view on the medium and long term prospects for the sector, predicated on strong fundamentals, current valuations levels and robust return expectations during rising interest rate environments. Lastly, in anticipation of expected Fed interest rate hikes in the U.S., the first of which occurred on December 16, and the concomitant impacts on the USD, they have maintained caution towards commodities. That said, given pricing dynamics and heightened volatility, they are attentive to potentially reducing that sustained underweight in the next quarter and continue to have the portfolio positioned to take advantage of the stabilization of oil prices through their energy high yield investment.

Hymans Robertson View

The team's approach to investing has not changed and Hymans acknowledge that many of the underlying asset classes in which the manager invests posted negative or flat returns in 2015 as a result of key macro themes, notably the China slowdown and its impact on commodities and emerging markets more broadly. In such an

environment, the portfolio will struggle to hit its long term target of LIBOR + 4% p.a. Returns last year were not unexpected. In more positive market conditions, the portfolio would be expected to materially exceed its performance target.

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 4.49% 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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