

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

Report to:	<b>Pensions Committee</b>
Date:	<b>19 July 2018</b>
Subject:	<b>Investment Management Report</b>

**Summary:**

This report covers the management of the Lincolnshire Pension Fund assets over the period from 1<sup>st</sup> January 2018 to 31<sup>st</sup> March 2018.

**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

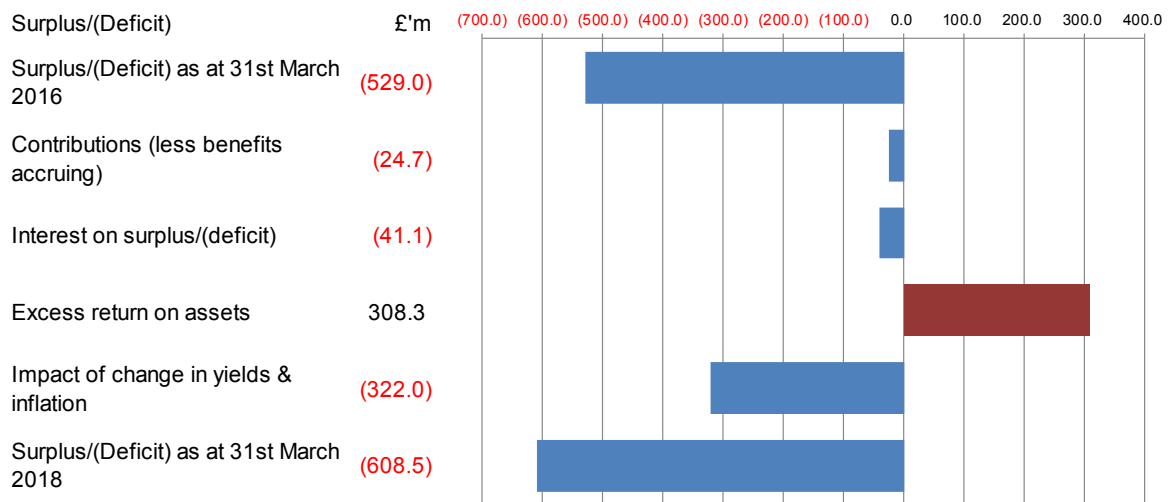
### **1. Funding Level Update**

- 1.1 The funding update is provided to illustrate the estimated development of the funding position of the Lincolnshire Pension Fund from the latest formal valuation, 31<sup>st</sup> March 2016, to the current quarter end, 31<sup>st</sup> March 2018. The accuracy of this type of funding update is expected to decline over time, as the period since the last valuation increases. This is because the funding update does not allow for changes in individual members' data since the last valuation. It is, however, a useful tool to assist the Committee to identify whether the time is right to reduce the overall risk in the asset allocation of the Fund, as it approaches a 100% funding level.
- 1.2 The graph over page shows the funding level at the latest formal valuation, at 76.9%, and its movement to 31<sup>st</sup> March 2018, where the funding level has increased to 78.6%. In terms of the funding level, 31<sup>st</sup> March was not a good point in time as stock markers were weak towards the end of quarter one 2018. If you move forward to the end of May 2018 the funding level has significantly improved to just less than 85.0%.

### Change in funding level since last valuation



1.3 Over the period 1<sup>st</sup> January to 31<sup>st</sup> March 2018 the deficit, in real money, has increased from £529m to £608.5m. The chart below shows the main impactors on the deficit. The excess return on assets has offset the negative changes in yields and inflation, interest on surplus/deficits and contributions being less than accruing benefits.



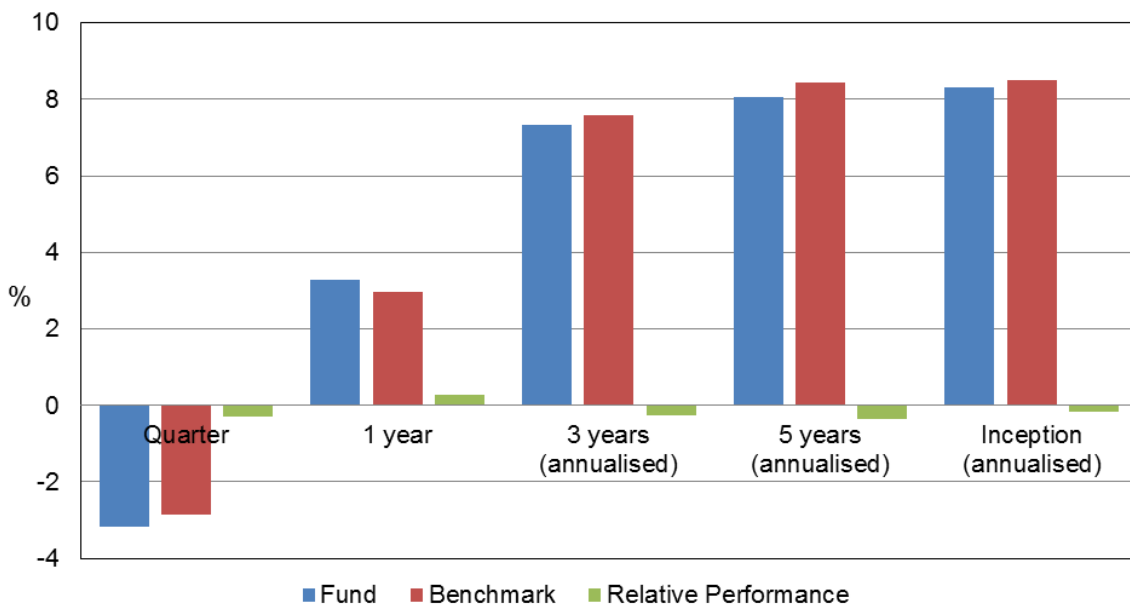
1.4 On a shorter term time horizon, looking at the last quarter, the funding level decreased from 82.1% to 78.6% between 31<sup>st</sup> December 2017 and 31<sup>st</sup> March 2018, and the deficit increased from £501m to £608.5m.

## 2. Fund Performance & Asset Allocation

2.1 The Fund decreased in value by £70.9m during the quarter from £2,246.0m to £2,175.1m, as the table below shows. The most significant movement in the quarter was seen on Global Equities which reduced in value by 3.0% or £45m.

Asset Class	Q1 2018 £m	Q4 2017 £m	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	404.0	433.7	18.6	20.0	(1.4)
Global Equities	936.2	981.1	43.0	40.0	3.0
Alternatives	312.3	310.4	14.4	15.0	(0.6)
Property	207.6	207.1	9.5	9.0	0.5
Infrastructure	35.4	32.7	1.6	2.5	(0.9)
Fixed Interest	264.1	265.5	12.1	13.5	(1.4)
Cash	15.5	15.5	0.7	0.0	0.7
<b>Total</b>	<b>2,175.1</b>	<b>2,246.0</b>	<b>100.0</b>	<b>100.0</b>	

2.2 The graph and table 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.



	Fund %	Benchmark %	Relative Performance %
Quarter	(3.16)	(2.86)	(0.30)
1 year	3.27	2.98	0.29
3 years*	7.32	7.59	(0.27)
5 years*	8.07	8.43	(0.36)
Inception**	8.32	8.50	(0.18)

\*Annualised from Yr 3. \*\*Since Inception figures are from March 1987

2.3 Over the quarter, the Fund produced a negative return of (3.16%) (as measured by JPMorgan), underperforming the benchmark by (0.3%). The Fund was ahead of the benchmark over the one year period, but behind its benchmark over three and five years, and since inception.

### 3. Hymans Robertson Manager Ratings

3.1 Hymans Robertson, as the Fund's Investment Consultant, regularly meets managers to discuss current issues, management changes and performance. Each 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. During the quarter there have been the following changes:

- Morgan Stanley Global Brands has moved from preferred to suitable. This change is not in response to any developments at the manager but part of the process of Hymans research team maintaining much smaller short lists of equity managers going forward. This reflects a preference from Hymans Robertson, on their consolidated list, for funds with more flexible investment strategies. They continue to support the investment philosophy behind this manager's strategy, which provides a degree of stability when employed alongside other active equity managers.
- RREEF Ventures Fund 3 has been removed as the fund has reached the end of its life now with only a nominal value remaining, so any research rating is not meaningful particularly as there is no follow-on vehicle from the manager.

3.3 Sixteen managers remained rated as retain positive or retain preferred. Two new managers Infracapital Greenfield Partners and Pantheon Global Infrastructure have been added to the assessment. Both have been rated as positive.

Manager	Rating				
	Replace		Retain – suitable	Retain – positive	Retain – preferred
Invesco Global Equities (Ex-UK)				X	
Columbia Threadneedle Global Equity				X	
Schroders Global Equity				X	
Morgan Stanley Global Brands			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	

Igloo Regeneration Partnership				X	
Aviva Pooled Property Fund				X	
Royal London PAIF				X	
Standard Life Pooled Property Fund				X	
Blackrock Property				X	
Infracapital Greenfield Partners I				X	
Pantheon Global Infrastructure				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 are shown in the table below. It was a poor quarter for the Fund with all but one manager showing negative absolute returns. Two managers, Morgan Stanley Global Brand and Morgan Stanley Alternative Investments underperformed their benchmark over the quarter. Over the 12 month period, all managers, except Morgan Stanley Global Brands have produced a positive absolute return, and have matched or outperformed their benchmark.

Manager	3 months ended 31 <sup>st</sup> March 2018			Previous 12 months			Target p.a. %
	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	
Legal & General (UK Equities)* <small>*From February 17</small>	(6.8)	(6.8)	0.0	1.4	1.4	0.0	Match Index
Invesco (Global Equities (ex UK))	(4.5)	(4.6)	0.1	1.8	1.3	0.5	+1.0
Columbia Threadneedle (Global Equities)	(3.3)	(4.4)	1.1	9.2	2.9	6.1	+2.0
Schroder's (Global Equities)	(4.1)	(4.5)	0.4	4.9	2.4	2.4	+3.0
Morgan Stanley Global Brands	(5.8)	(4.8)	(1.0)	(0.2)	1.3	(1.4)	n/a
Blackrock (Fixed Interest)	(0.5)	(0.5)	0.0	1.1	1.0	0.1	Match Index
Blackrock Interim (Fixed Interest)	(0.6)	(0.6)	0.0	0.4	0.4	0.0	Match Index
Morgan Stanley (Alternative Investments)	0.9	1.2	(0.2)	6.7	4.5	2.1	3M LIBOR + 4%

**Lincolnshire Pension Fund**  
**Global Equities – Invesco (Global Ex UK Enhanced)**  
**Quarterly Report March 2018**

**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 three factors: Momentum (Earnings and Price Momentum), Quality and Value.

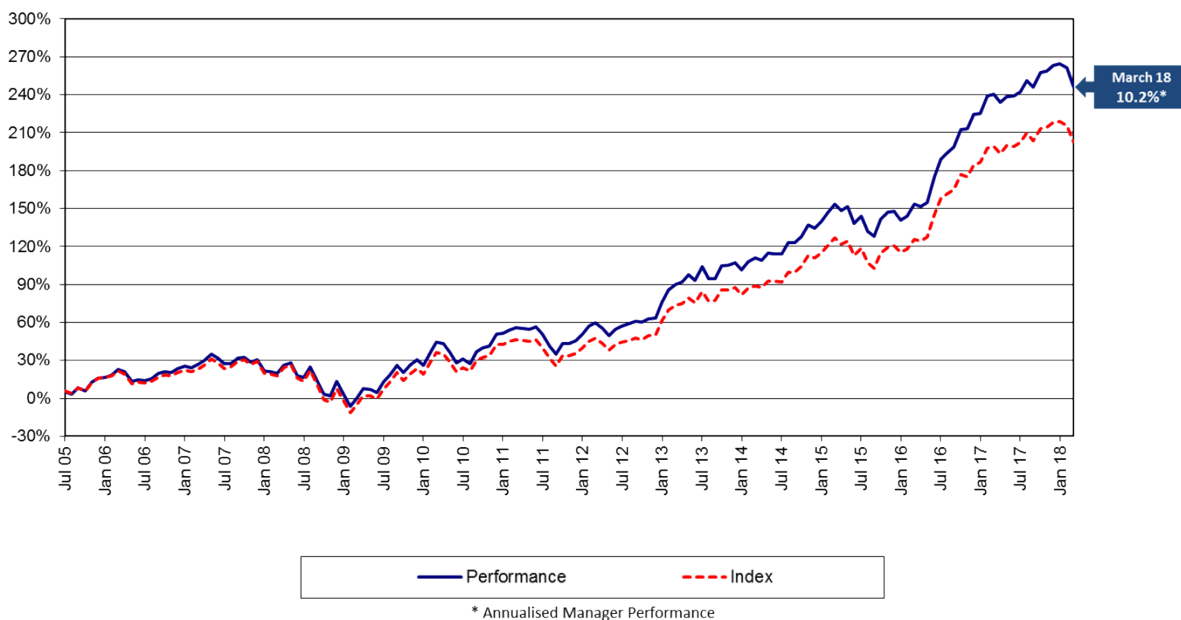
**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£524,978,456	£500,748,990

**Performance**

During the quarter Invesco's strategy outperformed its benchmark in two out of three months and was on the benchmark for the third month. As should be expected, stock selection led the outperformance with earnings momentum and value factors contributing to the positive performance. Performance over the longer term continues to be above the target return of +1%.

Invesco Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	(4.5)	1.8	11.0	12.8	10.2
MSCI World ex UK	(4.6)	1.3	10.1	11.8	9.1
Relative Performance	0.1	0.5	0.8	0.9	1.1

\* annualised, inception date 01/07/2005

## Turnover

Holdings at 31.12.17	Holdings at 31.03.18	Turnover in Qtr %	Turnover in Previous Qtr %
454	453	11.7	7.5

## Purchases and Sales

During the quarter, Invesco made a number of stock adjustments to the portfolio. Top purchases over the quarter included adding Dassault Aviation, Japan Post and Bouygues into the portfolio, and increasing their positions in Verizon, Dominion Bank and Marathon Petroleum. Top sales over the quarter came from selling out of positions in Sumitomo Mitsui and decreasing their positions in Sanofi, Canadian National Railway and Johnson and Johnson.

### Largest Overweights

Boeing	0.95%
Citigroup	0.82%
JP Morgan Chase	0.78%
Faurecia	0.77%
Walmart	0.74%

### Largest Underweights

Amazon	(0.69%)
Alphabet	(0.56%)
Visa	(0.41%)
Walt Disney	(0.41%)
DowDuPont	(0.40%)

\* Measured against MSCI World ex UK (NDR)

### Top 10 Holdings

1	Apple	£13,445,958
2	Microsoft	£9,659,207
3	JP Morgan Chase	£8,939,326
4	Boeing	£7,175,926
5	Citigroup	£6,604,248

6	Bank of America	£5,535,776
7	Walmart	£5,489,828
8	Facebook	£4,938,672
9	Novartis	£4,800,132
10	Alphabet	£4,742,180

## Hymans Robertson View

This is a quantitative global equity strategy run from Invesco's Frankfurt office. The team aims to implement a factor based strategy in a systematic manner – producing a well-diversified equity portfolio exhibiting a low level of volatility. The portfolio managers carry out a final check on the proposed portfolio/trades but the portfolio construction process is essentially carried out within the model. The strategy has been successful in generating modest levels of outperformance at very low levels of risk.

There were no significant developments over the quarter.

## Risk Control

The predicted tracking error of the portfolio slightly increased to 1.04%, compared to a target of 1%, with 94% of the active risk associated with Stock Selection Factors.

## Lincolnshire Pension Fund Global Equities – Schrodgers Quarterly Report March 2018

### 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. Schrodgers believe that stock markets are inefficient and they can exploit this by undertaking fundamental research and taking a long term view.

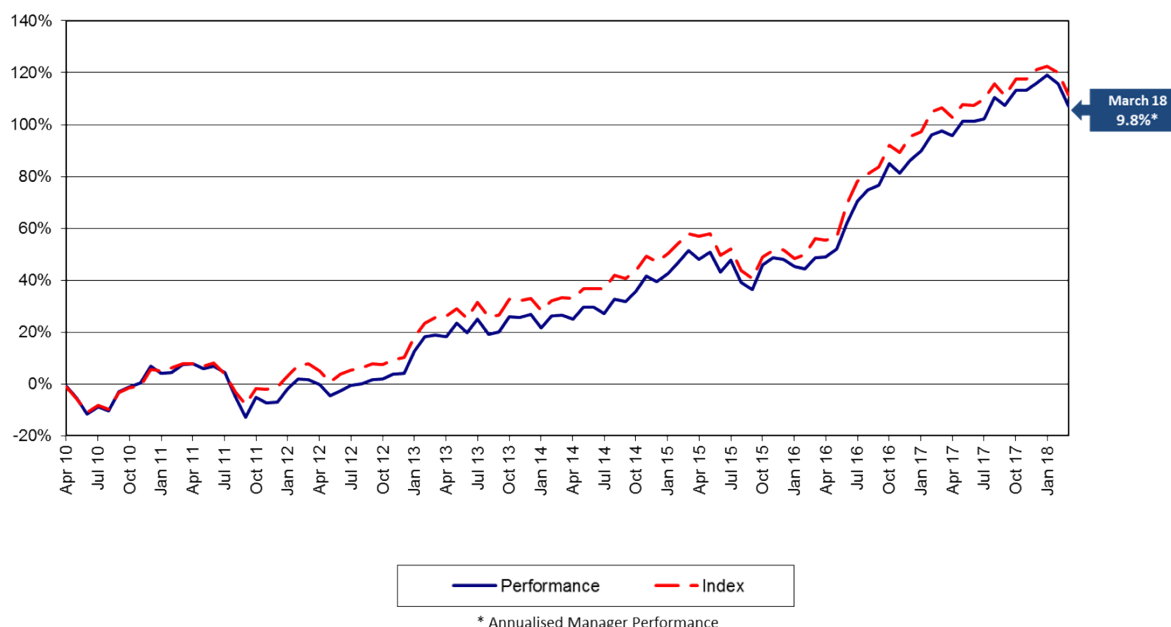
### Portfolio Valuation

Value at 31.12.17	Value at 31.03.18
£129,025,813	£123,755,393

### Performance

The portfolio outperformed the benchmark over the quarter and strongly outperformed over the year. Positions in the financial and consumer sectors – both discretionary and staples – contributed most significantly. There was also a benefit from an overweight in the IT sector. The only sector to pose a drag of any note was materials. Regionally, North America, emerging markets and Japan exposure delivered most of the positive excess returns but there were no regions of material weakness.

**Schrodgers Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception * %
Schrodgers	(4.1)	4.9	11.0	11.7	9.8
MSCI ACWI (Net)	(4.5)	2.4	10.2	11.0	10.1
Relative Performance	0.4	2.4	0.7	0.7	(0.3)

\*annualised, Inception date April 2010



## Turnover

Holdings at 31.12.17	Holdings at 31.03.18	Turnover in Qtr %	Turnover in Previous Qtr %
80	86	18.5	8.2

## Purchases and Sales

Several trades were made over the quarter; closing a number of positions as either the investment thesis played out or the stock deviated from the expectations for the business. Proceeds were rotated into higher conviction ideas. Citigroup was a key sale, and the holding rotated into Bank of America. Bayer was also sold due to its acquisition of Monsanto, which should work out in the long term, but there are risks of additional delays at this stage. At this point, more direct agricultural plays are preferred and a purchase in Deere was made accordingly. Elsewhere, purchases have been made in Adidas, which is increasing market share and expanding margins through efficiency improvements in its product delivery and capital use.

### Top 5 Contributions to Return

Estee Lauder	0.3%
Amazon	0.3%
Hewlett Packard	0.3%
Taiwan Semiconductor	0.2%
Raytheon	0.2%

### Bottom 5 Contributions to Return

Cimarex Energy	(0.3%)
Comcast	(0.2%)
DowDuPont	(0.2%)
Vodafone	(0.1%)
Procter & Gamble	(0.1%)

### Top 10 Holdings

1	Bank of America	£3,785,326
2	Alphabet	£3,644,365
3	Amazon	£3,605,908
4	JP Morgan	£3,323,044
5	Taiwan Semicont	£3,235,779

6	Visa	£2,899,187
7	United Health	£2,862,221
8	Estee Lauder	£2,678,013
9	PNC Financial Services	£2,600,666
10	Total (Energy)	£2,568,548

## Hymans Robertson View

The Schroder's fundamental equity team has settled down under the leadership of Alex Tedder. We regard his actions in rebuilding the team as being a good foundation for the future and should improve consistency. Although there have been periods in recent years when portfolios focused on fundamental long term growth have struggled in markets dominated by low growth and risk aversion, a more consistent performance record has now been established and we support the broad philosophy of the team.

## 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 – Columbia Threadneedle  
Quarterly Report March 2018**

**Investment Process**

The portfolio is designed to outperform the MSCI All Countries World Index by 2% per annum, gross of fees, over rolling three-year periods. The team focus on quality growth companies with high or rising returns on investor capital, and sustained or improving competitive advantage. The focus is on stock selection, with a well-diversified portfolio designed to deliver superior risk adjusted returns.

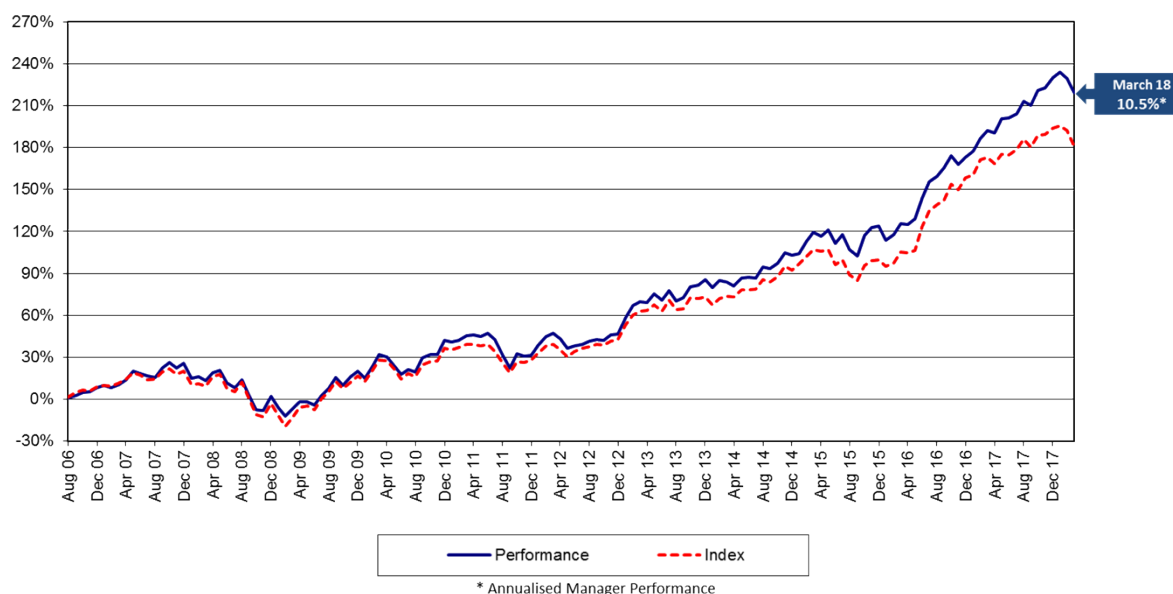
**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£137,499,819	£132,967,366

**Performance**

Gross of fees, the fund outperformed its index over the quarter and individually in two out of three of the months. Stock selection drove returns, led by picks in consumer staples and technology. Sector allocations also contributed to performance, with zero weights in utilities and the real estate sectors. Top contributors included: Amazon as investors remain positive about the company's cloud demand fundamentals; MasterCard, from the e-commerce momentum and Brazilian digital payments company PagSeguro IPO. Detractors included: Alphabet and Facebook, concerns over data security and associated regulation prompted the rotation out of these names in March.

Columbia Threadneedle Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception * %
Columbia Threadneedle	(3.3)	9.2	13.3	13.5	10.5
MSCI ACWI	(4.4)	2.9	10.8	11.5	9.3
Relative Performance	1.1	6.1	2.3	1.7	1.1

\* annualised, inception date 01/08/2006

## Turnover

Holdings at 31.12.17	Holdings at 31.03.18	Turnover in Qtr %	Turnover in Previous Qtr %
81	80	7.8	12.7

## Purchases and Sales

New positions were initiated in: Siam Commercial Bank, an attractively-valued, full service Thai bank, which stands to benefit from a decrease in credit costs and loan growths; PagSeguro Digital a Brazilian digital payments firm with a branded, self-serve distribution channel that competitors would struggle to replicate; and Equinix an internet connection specialist. This was funded by the exit from multinational off-price apparel retailer TJX Companies, and reallocating away from positions held in biopharmaceutical innovator Pfizer and multinational food and beverage company PepsiCo.

### Top 5 Contributions to Return

Amazon	0.42%
PagSeguro Digital	0.30%
Estee Lauder	0.22%
Nintendo	0.22%
Mastercard	0.22%

### Bottom 5 Contributions to Return

Dentsply Sirona	(0.34%)
Macom Technology	(0.34%)
Facebook	(0.23%)
Sekisui Chemical	(0.23%)
Osram Licht	(0.22%)

### Top 10 Holdings

1	Alphabet	£4,552,316
2	Amazon	£3,922,956
3	JP Morgan	£3,845,706
4	Alibaba	£3,513,452
5	Microsoft	£3,323,053

6	CRH Plc	£3,218,212
7	Bank of America	£3,178,918
8	Unilever	£3,052,103
9	Mastercard	£3,006,535
10	Charles Schwab	£2,937,038

## Hymans Robertson View

The team's investment approach is based on fundamental research with a strong emphasis on inputs from the broader investment research resources at Columbia Threadneedle. The portfolios of around 60 - 70 stocks typically have a growth bias. The team is now well resourced and will hopefully enjoy a period of stability. William Davies is regarded as key to the operation of the team and we will be monitoring whether his expanded role as Head of Equities for EMEA has any detrimental impact in terms of his time spent on portfolio management.

There were no significant developments over the quarter.

## 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 2018**

**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.

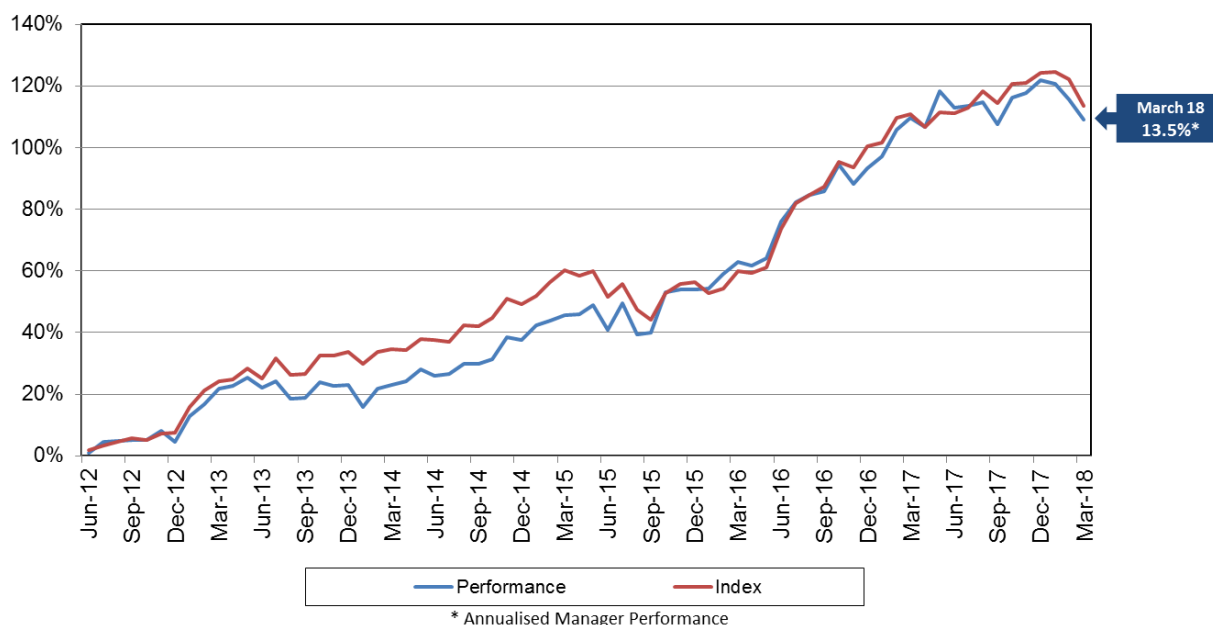
**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£189,592,648	£178,714,621

**Performance**

The portfolio underperformed in relative terms over the quarter, returning -5.8% versus -4.8% for the index. Sector allocation was neutral, as the benefits from overweight information technology and the absence of energy stocks was balanced by the drag from consumer staples being overweight. The largest contributors in absolute performance in the quarter were: Zoetis, Microsoft and Twenty-First Century Fox. The largest detractors were British American Tobacco, Reckitt Benckiser and RELX.

**Morgan Stanley Global Brands Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	(5.8)	(0.2)	12.9	11.4	13.5
MSCI World Index	(4.8)	1.3	10.0	11.5	13.9
Relative Performance	(1.0)	(1.4)	2.6	0.0	(0.3)

\*annualised, inception date 18/06/2012

## Purchases and Sales

During the quarter, positions were initiated in Heineken and Abbott Laboratories. Heineken, the global beer player, has sharply improved under a new CEO and is now more balanced in terms of brand and geography. Abbott Laboratories, a global health care company, has a diverse range of high-quality businesses, including medical devices, diagnostics, branded nutritional products and branded pharmaceuticals sold into emerging markets. The exit from Nestle was completed in this quarter and the position in Disney was reduced as the proposed merger with 21<sup>st</sup> Century Fox made the position size in the combined entity too large.

### Top Contributors to Return

Zoetis	0.47%
Microsoft	0.26%
Twenty-First Century Fox	0.13%

### Bottom Contributors to Return

British American Tobacco	(1.50%)
Reckitt Benckiser	(0.76%)
RELX	(0.58%)

### Top Ten Holdings

Company	Industry	% Weighting
Reckitt Benckiser	Household Products	8.07
British American Tobacco	Tobacco	7.95
Unilever	Personal Products	7.49
Microsoft	Software	6.55
Accenture	IT Services	6.49
Visa	IT Services	4.66
Twenty-First Century Fox	Media	4.52
Philip Morris	Tobacco	4.40
L'Oreal	Personal Products	4.25
SAP	Software	4.16

### Hymans Robertson View

The manager runs concentrated portfolios of 20 - 40 stocks with a strong quality bias, low turnover and low volatility in absolute terms. Companies need to exhibit high returns on capital, be investing to protect their brands and have shareholder friendly management teams. There is a tendency for the portfolio to have very high allocations to consumer and technology stocks, often with limited or no exposure to many other sectors of the market. The decision to change the rating merely reflects a preference in the research team's consolidated list of funds for more flexible investment strategies. It is still regarded as an appropriate strategy to be held within a diversified active manager line-up.

We have changed our rating for the Morgan Stanley Global Franchise (Brands) strategy from 'Preferred' to 'Suitable'. This change is not in response to any developments at the manager but part of the process of our research team maintaining much smaller short lists of equity managers going forward.

**Lincolnshire Pension Fund  
UK Equities – Legal & General (LGIM)  
Quarterly Report March 2018**

**Investment Process**

This pooled fund employs a tracking strategy, aiming to replicate the performance of the FTSE All-Share Index to within +/-0.25% p.a. for two years out of three. The fund follows a pragmatic approach to managing an index fund, either investing directly in the securities of that index or indirectly through other LGIM funds. The fund may also hold index and single stock futures for efficient portfolio management.

**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£433,567,930	£403,792,800

**Performance**

Over all periods the portfolio has performed as expected.

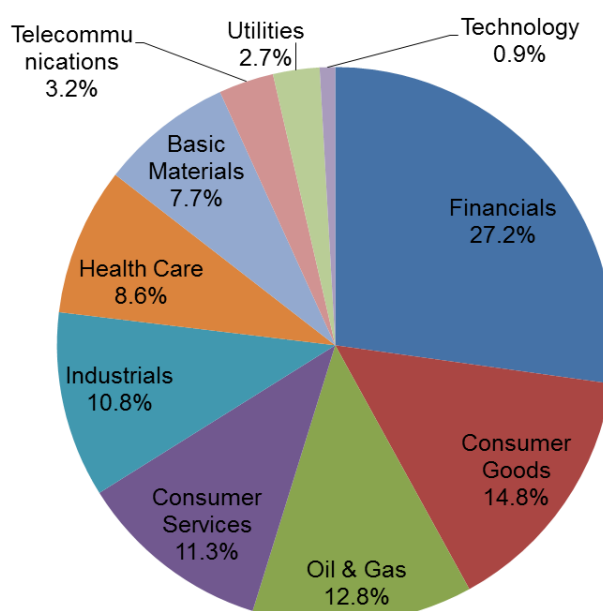
	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
LGIM	(6.9)	1.3	n/a	n/a	3.0
Benchmark	(6.9)	1.2	n/a	n/a	2.7
Relative Performance	0.0	0.1	n/a	n/a	0.2

\*annualised, inception date February 2017

**Top Ten Holdings**

Company	% Weighting
Royal Dutch Shell A	8.3
HSBC Holdings	5.9
British American Tobacco	4.1
BP	4.1
GlaxoSmithKline	3.0
Astrazeneca	2.7
Diageo	2.6
Vodafone Group	2.3
Lloyds Banking Group	2.0
Prudential	2.0
<b>Total</b>	<b>37.0</b>

**Whole Fund Sector Breakdown**



**Lincolnshire Pension Fund  
Passive Bonds – Blackrock  
Quarterly Report March 2018**

**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 All Stocks UK Gilt Index Fund	Sampled

**Portfolio Valuation at 31<sup>st</sup> March 2018**

<b>Portfolio</b>	<b>31.12.17 £</b>	<b>31.03.18 £</b>
Corporate Bond All Stocks Index Fund	68,867,424	68,069,339
Over 5 Years UK Index-Linked Gilt Index Fund	42,165,987	42,252,449
All Stocks UK Gilts*	27,406,875	27,482,479
Cash (residual)	1	1
<b>Total</b>	<b>138,440,288</b>	<b>137,804,268</b>

\*Switched from Overseas Bond Index Fund in February 17

**Performance**

Over all periods the portfolio has performed as expected.

	<b>Quarter %</b>	<b>1 Year %</b>	<b>3 Year* %</b>	<b>5 Year* %</b>	<b>Inception* %</b>
Blackrock	(0.5)	1.1	5.8	5.8	7.2
Composite Benchmark	(0.5)	1.0	5.7	5.7	7.1
Relative Performance	0.0	0.1	0.1	0.1	0.1

\*annualised since inception 28/07/10

**Hymans Robertson View**

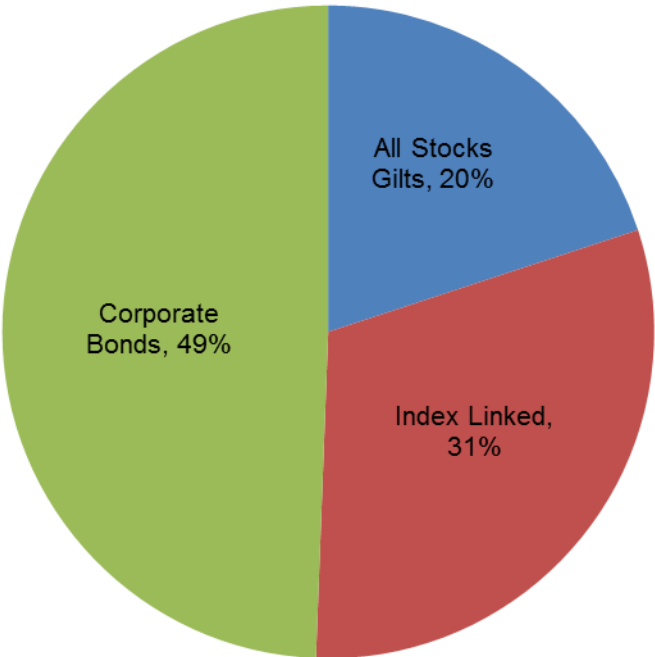
There were no significant developments within the Index Fixed Income team over the quarter.

**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 All Stocks UK Gilt Index Fund	20%

The pie chart below shows the allocation as at 31<sup>st</sup> March 2018.





**Lincolnshire Pension Fund**  
**Passive Bonds – Blackrock interim**  
**Quarterly Report March 2018**

**Investment Process**

Since the termination of BMO's Absolute Return bond fund, that element of the Fund's asset allocation has been temporarily housed in an interim Blackrock fund of short dated corporate bonds. The fund is managed passively, and aims to achieve index returns in line with the iBoxx Sterling Non-Gilts 1-5 Year Index.

**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£127,064,948	£126,292,803

**Performance**

Over all periods the portfolio has performed as expected.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock Interim	(0.6)	0.4	n/a	n/a	0.9
Benchmark	(0.6)	0.4	n/a	n/a	0.8
Relative Performance	0.0	0.0	n/a	n/a	0.1

\*annualised since inception 14/09/16

**Hymans Robertson View**

We rate BlackRock's index-tracking equity capability at 'Preferred'. There were no significant developments over the quarter.

**Lincolnshire Pension Fund  
Alternative Investments – Morgan Stanley  
Quarterly Report March 2018**

**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 Fund allocation. The manager has a target to beat the return of 3 Month LIBOR + 4%. Morgan Stanley also manage the legacy private equity investments, however they are excluded from this report.

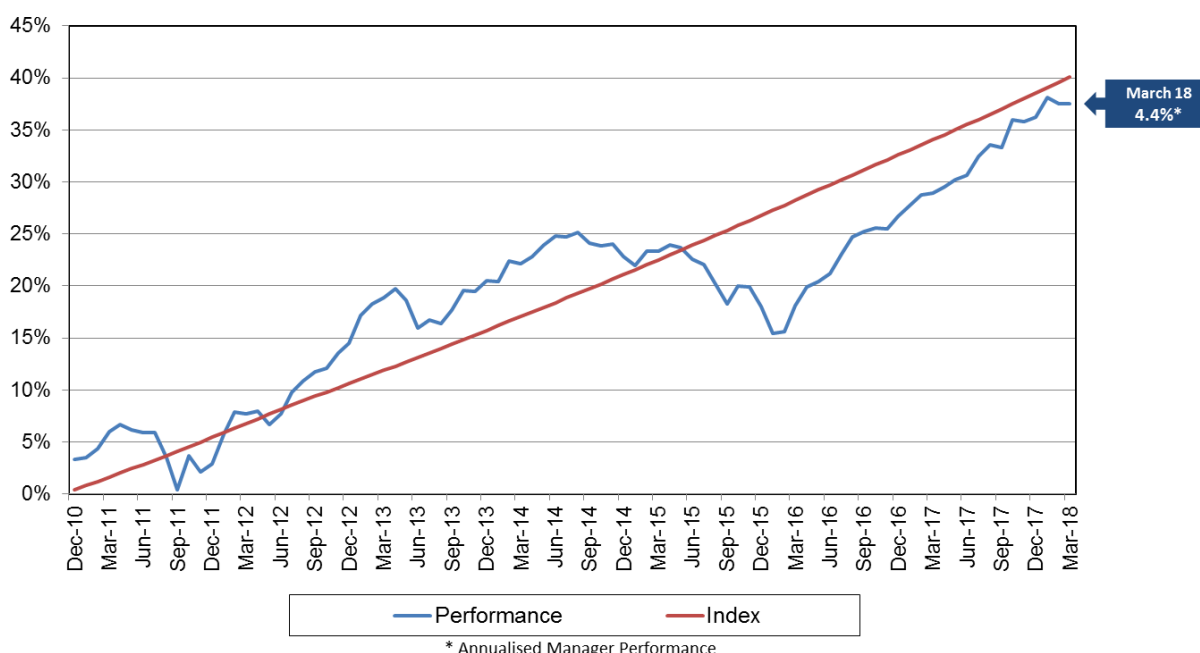
**Portfolio Valuation**

Value at 31.12.17	Value at 31.03.18
£273,986,004	£280,714,740

**Performance**

The portfolio underperformed during the quarter. Positive contributions from private markets, frontier equity and, to a lesser extent, hedge funds, offset declines across credit and listed real assets. Tactical decisions were muted, while manager selection modestly detracted from relative returns. Within manager selection, frontier equity, hedge funds and senior loans particularly lagged.

**Morgan Stanley AIP Performance Since Inception**



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	0.9	6.7	3.7	3.0	4.4
3 Month LIBOR + 4%	1.2	4.5	4.6	4.6	4.7
Relative Performance	(0.2)	2.1	(0.8)	(1.6)	(0.3)

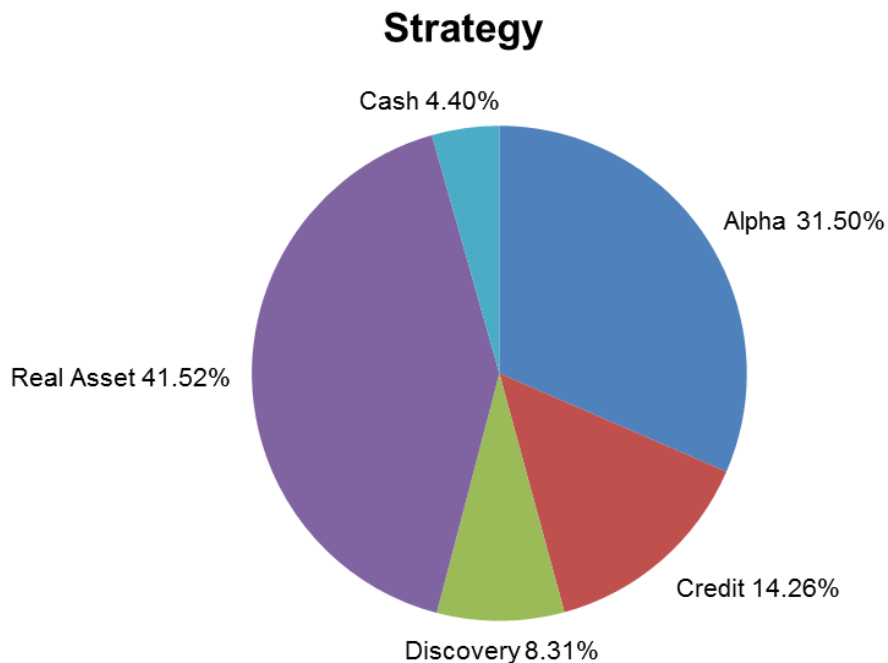
\* annualised since inception date 24/11/2010

## Allocation

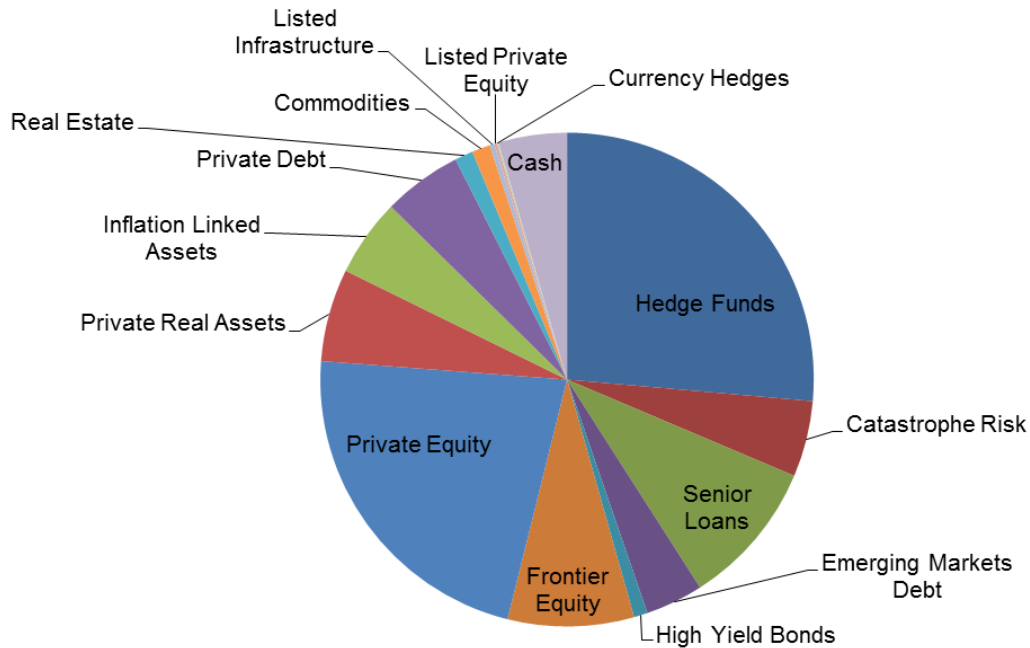
Morgan Stanley has split out investments into a bespoke portfolio of alternatives comprising five different asset allocations:

- **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.

The pie charts below show the strategy and asset class positions of the Morgan Stanley portfolio as at 31<sup>st</sup> March 2018.



## Asset Class



### Portfolio Outlook

While 2017 was marked by a period of systemically low financial market volatility, reflecting the impact of extremely active monetary policies by the global central banks, 2018 has started in a very different manner. A combination of higher inflation expectations, a consequent gradual tightening of monetary policy, a slight softening of economic growth expectations and a pick-up in idiosyncratic news flow has meant that the first quarter of 2018 has been marked by materially higher financial market volatility. This has been reflected across all risk markets, and credit spreads have widened materially. However, technicals remain generally strong across credit markets, and MS anticipate that they will continue to support credit as a whole.

MS envision an improved environment for alpha. The correlation environment should remain supportive of security selection and global macro strategies. Low intra-stock correlations globally should facilitate continued strong alpha generation for fundamental and quantitative equity long/short strategies, while low cross-asset and cross-region correlations allow macro strategies to build portfolios with numerous return drivers. MS remain constructive on equity event-driven strategies, as a positive outlook for mergers and acquisitions activity in conjunction with the favourable stock picking environment supports a robust opportunity set. MS continue to emphasize strategies that can perform well in the current benign market environment and can successfully manage a potential regime shift, with a focus on alpha-centric strategies.

Within private real assets, MS recently made a co-investment alongside a high conviction manager in the acquisition, renovation and lease-up of a student housing asset in Ireland. MS remain disciplined in small and mid-cap private equity bias and have a consistently strong flow of attractive co-investment opportunities with high quality partners. During the quarter, the portfolio closed on another fund restructuring transaction that was focused on a market leading company in the oral healthcare products industry. MS are currently evaluating several opportunities

that they believe will offer a similar return premium due to complexity and time constraints.

### **Hymans Robertson View**

This strategy offers exposure to a broad range of alternative assets. Morgan Stanley employs an open architecture approach, investing through both internal and external fund managers. For liquidity purposes the portfolio has historically maintained a high allocation to hedge funds. In addition, the strategy is designed to remain fully invested and the manager will not make active use of cash or fixed income to preserve capital during stress periods in markets.

There were no significant developments over the quarter.

### **Risk Control**

Portfolio volatility since inception is 3.65%, within the guidelines specified by the mandate.

## **Conclusion**

Over the quarter, the Fund produced a negative return of (3.16%), slightly underperforming the benchmark which returned (2.86%).

## **Consultation**

### **a) Have Risks and Impact Analysis been carried out?**

Yes

### **b) Risks and Impact Analysis**

The Pension Fund has a Risk Register which can be obtained by contacting the author of this report.

## **Background Papers**

This report was written by Claire Machej, who can be contacted on 01522 553641 or [claire.machej@lincolnshire.gov.uk](mailto:claire.machej@lincolnshire.gov.uk).