

Regulatory and Other Committee

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

Report to:	Pensions Committee
Date:	09 October 2014
Subject:	Performance Measurement Annual Report

Summary:

This report sets out the Pension Fund's longer term investment performance, for the periods ending 31st March 2014.

Recommendation(s):

That the Committee note the report.

Background

1 INTRODUCTION

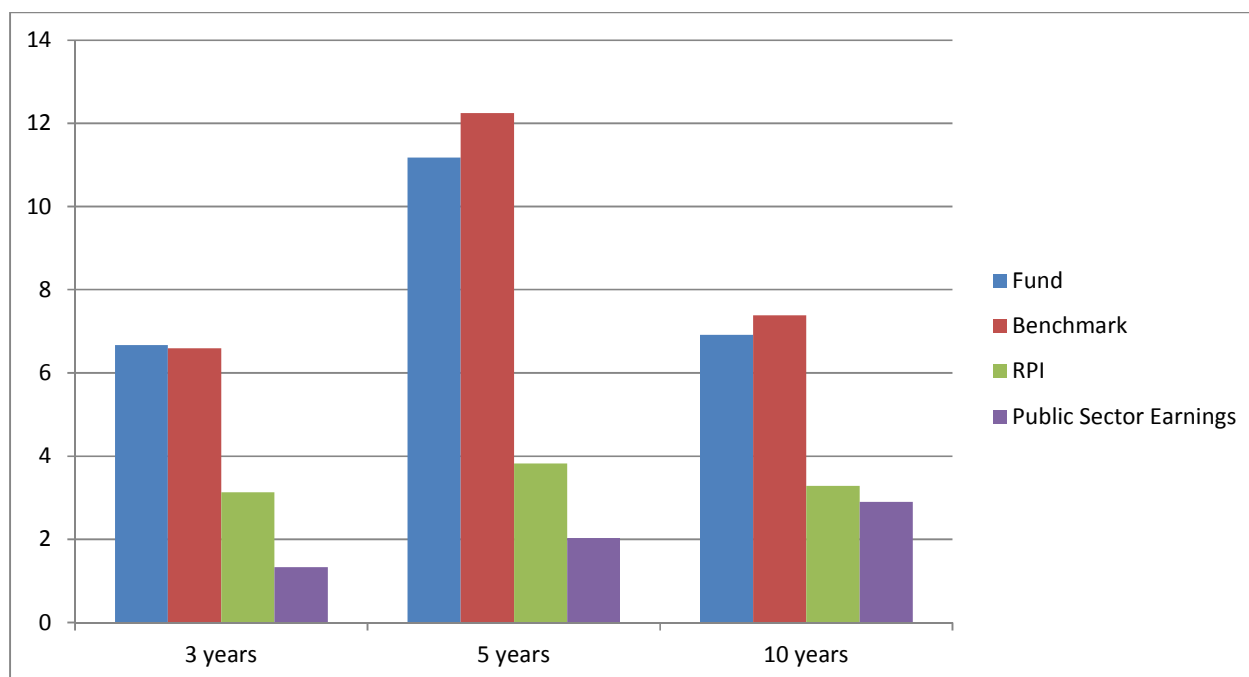
- 1.1 The Pension Fund uses two suppliers for the measurement of the Fund's performance. JPMorgan, the Fund's custodian, calculates the Fund's investment performance and compares it with the returns of the strategic asset allocation benchmark (i.e. the return achieved by the mix of assets as recommended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

2 LONGER TERM PERFORMANCE FOR YEARS ENDED 31 MARCH 2014

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

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

INFLATION INCREASES AND INVESTMENT RETURNS FOR UP TO 10 YEARS ENDED 31/3/2014



	3 years annualised %	5 years annualised %	10 years annualised %
Retail Prices Index increases	3.1	3.8	3.3
Public sector average Earnings increases	1.3	2.0	2.9
LCC Fund performance	6.7	11.2	6.9
LCC Benchmark Performance	6.6	12.3	7.4
Relative Performance	0.1	(0.9)	(0.4)

2.3 10 Year Returns

The Fund's performance over ten years, at 6.9%, is slightly behind the Fund's Benchmark return of 7.4%. This return is ahead of both inflation and average earnings over the last ten years, to which the scheme's liabilities are linked, which were 3.3% and 2.9% p.a. The Fund's performance

reflects poor stock selection by the Fund's active asset managers over a number of years, as can be seen in the table at paragraph 3.4.

2.4 5 Year Returns

Five year returns of 11.2% per annum are ahead of both price and pay inflation. The Fund's actual performance is behind the strategic Benchmark return of 12.3%. This reflects the underperforming active managers, and the shift away from the strategic benchmark position in 2009 and 2010, ahead of the transitions to the new benchmark in 2010.

2.5 3 Year Returns

Three year returns, at 6.7%, are ahead of both inflation and average earnings, and marginally ahead of the strategic benchmark return of 6.6%.

3 ATTRIBUTION ANALYSIS

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

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

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

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

Long Term Performance Analysis

Year ended March	Fund %	Benchmark %	Relative Performance %	Attributed to Asset allocation %	Attributed to Stock Selection %
2005	11.0	11.9	(0.8)	0.2	(1.0)
2006	24.4	24.1	0.3	0.7	(0.4)
2007	6.9	6.5	0.3	0.4	(0.1)
2008	(4.4)	(3.3)	(1.1)	0.1	(1.2)
2009	(18.6)	(20.0)	1.7	2.1	(0.4)
2010	29.7	36.7	(5.1)	(3.1)	(2.1)
2011	7.9	7.8	0.1	0.1	0.0
2012	1.5	2.4	(0.8)	(0.2)	(0.6)
2013	12.6	11.3	1.2	0.12	1.04
2014	6.3	6.2	0.1	0.15	(0.08)

4 WM LOCAL AUTHORITY UNIVERSE

- 4.1 The WM Company (a wholly owned subsidiary of State Street) measures the performance of the Fund against the Local Authority Universe. The WM Local Authority (LA) Universe is an aggregation of 84 funds within the LGPS sector that are used for peer group comparisons.
- 4.2 The weighted average return for Local Authority Pension Funds in the WM Local Authority Universe over the year 2013/14 was 6.4%, slightly ahead of the Lincolnshire Fund return of 6.3%. The actual performance of the Fund ranked in the middle of the Local Authority funds, at the 54th percentile. Over the longer term, the Fund is in the 70th to 80th percentile.
- 4.3 The table below shows how the asset allocation for the Lincolnshire Fund compares with the average Local Authority Pension Fund in 2014 and 2013.

Asset Class	Lincolnshire	LA Average	
		2014	2013
Equities	60.0	63	63
Bonds	13.5	16	18
Property	11.5	8	7
Alternatives	15.0	10	9
Cash	0.0	3	3

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

Paper 11 of this committee brings further discussion on the asset allocation beneath these areas.

- 4.5 Within the LA Universe, there has been a reduction in bonds and an increase in alternatives and property. Within equities, the move from UK to global equities has continued, although the overall allocation has remained static.
- 4.6 Additional research on active management from WM, to the year ended December 2013, has shown that UK equity managers have generally outperformed their benchmarks in the last four years. Global equity managers have not fared so well, with performance being more mixed and generally less positive. There has also been a move away from segregated mandates to pooled funds, possibly as a result of the onerous and costly OJUE requirements in selecting a segregated manager.

Conclusion

- 5.1 The Pension Fund's investment performance of 6.9% over the 10 year period ended 31st March 2014 was slightly behind the strategic benchmark of 7.4%. The Fund is seeking to outperform the Benchmark by 1% per annum over rolling three year periods. Annualised returns over three, five and ten year periods are ahead of inflation in pay and prices. At an absolute level, the ten year performance is comfortably ahead of the current actuarial assumption for return of around 5% per annum.
- 5.2 Looking at the individual years, there was a positive contribution from asset allocation and a negative contribution from stock selection in the year ended March 2014. In eight of the last ten years, stock selection has detracted from performance.

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 Jo Ray, who can be contacted on 01522 553656 or jo.ray@lincolnshire.gov.uk.

