

Regulatory and Other Committee

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

Report to:	Pensions Committee
Date:	08 January 2015
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 2014.

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

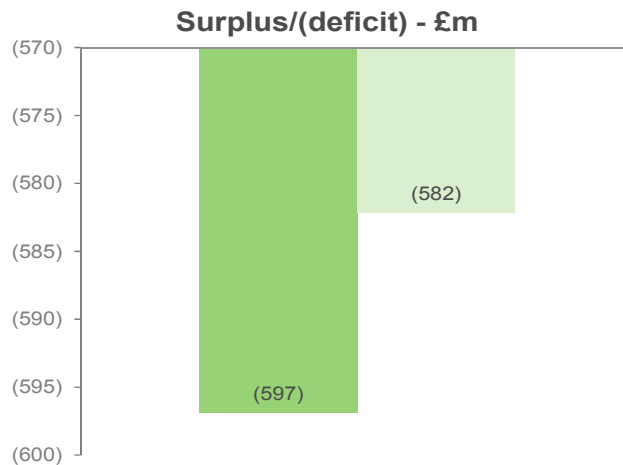
1. Funding Level Update

- 1.1 The funding update is provided to illustrate the estimated development of the funding position from 31st March 2013 to 30th September 2014, 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 2014 the funding level has increased to 73.8%. This is largely as a result of good investment performance.
- 1.3 In the period since 30th June 2014, the funding level has fallen from 76.8% to 73.8% as a result of the recent fall in government bond yields.

Change in funding level since last valuation



- 1.4 As shown below, the deficit in real money has reduced from £597m to £582m between the period 31st March 2013 and 30th September 2014. The deficit at 30th June 2014 was £488m.



2. Fund Performance & Asset Allocation

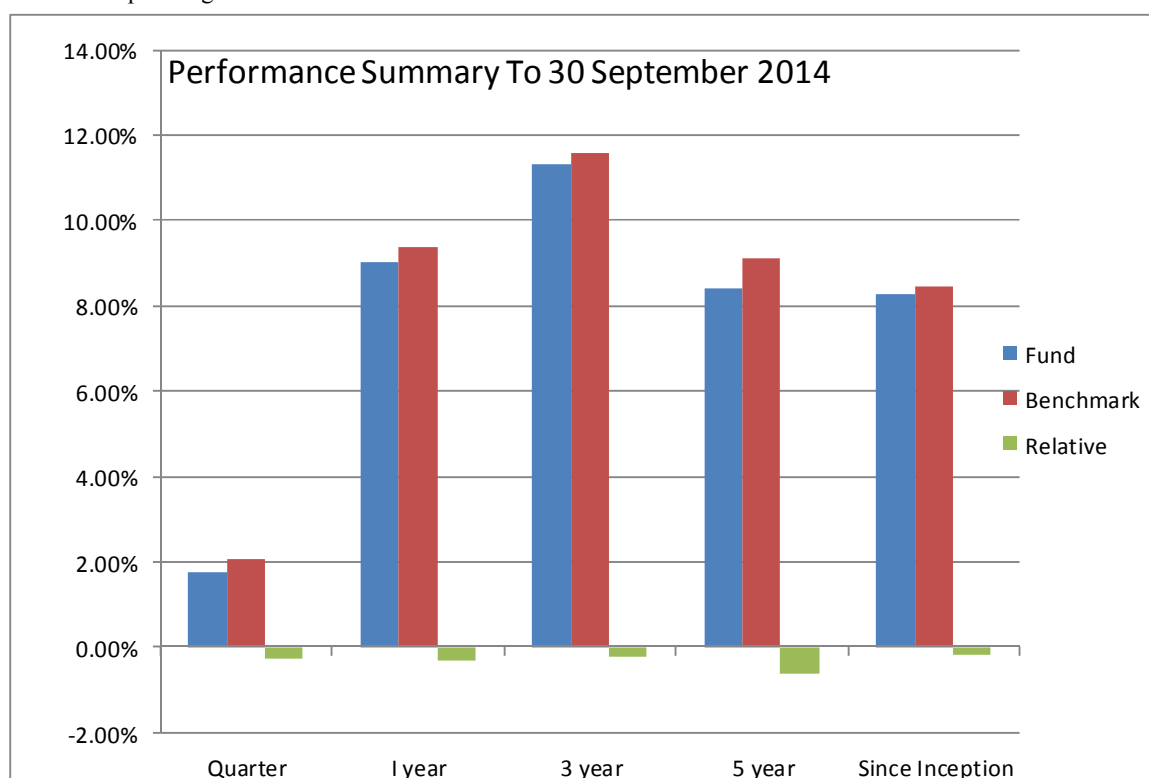
- 2.1 The Fund increased in value by £28.3m during the quarter from £1,618.7m to £1,647m, as the chart below shows. The Fund was overweight to cash and global equities and underweight UK equities, fixed interest, alternatives and property.

Asset Class	Q3 2014 £	Q2 2014 £	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	318.9	326.5	19.4	20.0	(0.6)
Global Equities	690.7	671.7	41.9	40.0	1.9
Alternatives	235.0	230.9	14.3	15.0	(0.7)
Property	185.7	182.5	11.2	11.5	(0.3)
Fixed Interest	202.4	201.4	12.3	13.5	(1.2)
Cash	14.3	5.7	0.9	0.0	0.9
Total	1,647.0	1,618.7	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 1% per annum.

2.3 Over the quarter, the Fund produced a positive return of 1.77% underperforming the benchmark which returned 2.05%. 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 has been no change in the rating of any of these managers over the quarter. Hymans Robertson still rate sixteen managers as retain and have categorised three managers, Reef Property Ventures Fund 3, Aviva Pooled Property Fund and Schroders, as "on watch" and Neptune as "strongly on watch". Officers will monitor these managers closely and arrange meetings to discuss any potential issues. In December Schroders, Neptune and Threadneedle attended the Pensions Committee for their annual presentation. The committee discussed performance and future expectations of the managers. These discussions fed into the asset allocation meeting later that day which is summarised in agenda item 8.

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 mixed quarter for the Fund with six of the nine managers producing a positive absolute return. Over the quarter three managers outperformed their benchmark and two matched their benchmark. Schroder's, Morgan Stanley Global Brands, F&C and Morgan Stanley Alternative Investments all underperformed their benchmark over the quarter. Over the 12 month period all managers have produced positive absolute returns and only four of the managers underperformed against the

index. Against their target, only the in house team, Invesco, Morgan Stanley Alternatives and Blackrock have matched or beaten the required return.

	3 months ended 30/09/14			Previous 12 months			
Manager	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	Target p.a. %
Passive UK Equity In house	(1.1)	(1.1)	0.0	5.8	5.6	0.1	+/- 0.5
Invesco (Global Equities (ex UK))	4.1	3.6	0.5	14.8	12.7	1.8	+1.0
Threadneedle (Global Equities)	3.4	3.2	0.2	12.1	11.8	0.3	+2.0
Neptune (Global Equities)	4.0	3.2	0.8	8.9	11.8	(2.6)	+4.0
Schroder's (Global Equities)	1.8	3.0	(1.2)	9.7	11.2	(1.4)	+3.0
Morgan Stanley Global Brands	3.1	3.2	(0.1)	9.2	12.1	(2.6)	n/a
Blackrock (Fixed Interest)	3.6	3.6	0.0	6.7	6.7	0.0	Match Index
F&C (Fixed Interest)	(2.5)	0.9	(3.4)	2.4	3.6	(1.1)	3M LIBOR + 3%
Morgan Stanley (Alternative Investments)	(0.6)	1.2	(1.7)	5.4	4.6	0.8	3M LIBOR + 4%

Lincolnshire Pension Fund
UK Equities – In House (Passive UK)
Quarterly Report September 2014

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.

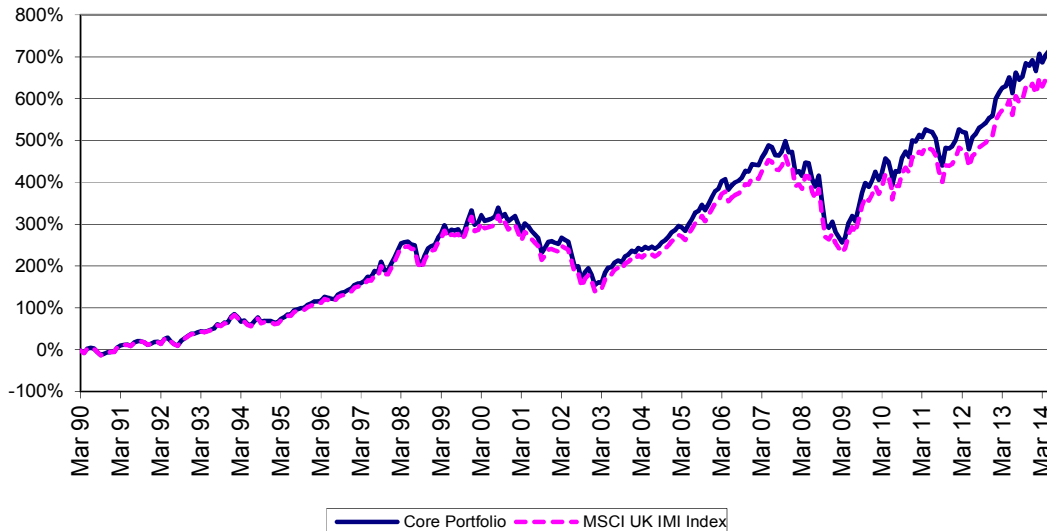
Portfolio Valuation

Value at 30.06.14	Value at 30.09.14
£326,491,228	£318,884,035

Performance

During the quarter the portfolio produced a negative return of 1.1% which matched the index. This was achieved through the portfolio's underweight positioning in Information Technology and materials whilst detractors to performance were underweight positions in financials and healthcare and an overweight position in energy. Over all other periods the portfolio has slightly outperformed the index and is within the target of +/- 0.5%.

UK Equities In House Portfolio Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
UK Equities – In House	(1.1)	5.8	13.8	9.8	8.6
MSCI UK IMI	(1.1)	5.6	13.8	9.7	8.3
Relative Performance	0.0	0.1	0.1	0.1	0.3

* annualised, inception date 01/10/1989

Turnover

Holdings at 30.06.14	Holdings at 30.09.14	Turnover in Quarter %	Turnover in Previous Quarter %
247	249	0.1	0.9

Purchases and Sales

During the quarter there was little activity within the portfolio with a single trade being undertaken to increase the fund's holding in Lloyds. This was done to reduce the underweight position to both Lloyds and the financial sector.

Largest Overweights

Vodafone Group	0.15%
BP	0.13%
Rio Tinto	0.12%
British American Tobacco	0.12%
Royal Dutch Shell	0.10%

Largest Underweights

Lloyds Banking	(0.18%)
Shire PLC	(0.15%)
Barclays	(0.13%)
Astrazeneca	(0.09%)
Intu Properties	(0.09%)

* Measured against MSCI UK IMI

Top 10 Holdings

1	Royal Dutch Shell	£25,112,862
2	HSBC Holdings	£19,719,150
3	BP	£14,065,846
4	GlaxoSmithkline	£11,760,930
5	British American Tobacco	£11,091,598

6	Vodafone Group	£9,329,311
7	Astrazeneca	£8,891,883
8	Diageo	£7,594,859
9	Rio Tinto	£6,635,984
10	Lloyds Banking Group	£6,626,857

Risk Control

The portfolio has a tracking error limit of 0.5%. At the end of September 2014 the tracking error was 0.25%.

Lincolnshire Pension Fund
Global Equities – Invesco (Global Ex UK Enhanced)
Quarterly Report September 2014

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.

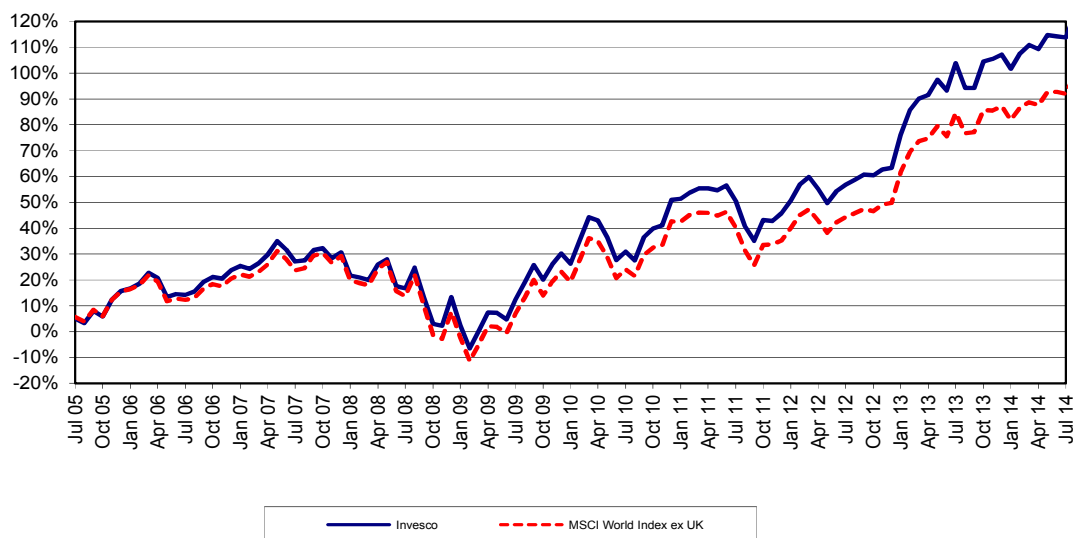
Portfolio Valuation

Value at 30.06.14	Value at 30.09.14
£338,749,574	£347,438,525

Performance

During the third quarter Invesco's strategy outperformed its benchmark. Stock Selection had the largest positive impact on relative performance, as the contribution from their overweighted assets was positive. In addition, intended overweight's in stocks with a high earnings expectation score added to performance. Contributions from Countries and Currencies, which are a residual of their Stock Selection, were slightly negative. Overweights in New Zealand stocks helped performance, while overweights in Danish stocks hurt performance.

Invesco Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	4.1	14.8	18.2	12.1	9.1
MSCI World ex UK	3.6	12.7	16.7	10.7	7.8

Relative Performance	0.5	1.8	1.3	1.3	1.2
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* annualised, inception date 1st July 2005

Turnover

Holdings at 30.06.14	Holdings at 30.09.14	Turnover in Quarter %	Turnover in Previous Quarter %
435	417	7.5	7.7

Purchases and Sales

During the quarter Invesco made a number of stock adjustments to the portfolio as a result of their Stock Selection model. They added Coca-Cola and increased their positions in NTT, Hennes & Mauritz, Trinity Industries and Liberty Ventures. These were funded by selling out of Lowe's, Monsanto and UPM and reducing positions in Hutchinson Whampoa and Procter & Gamble.

Largest Overweights

Archer Daniels	1.01%
Northrop Grumman	1.01%
NTT	0.98%
Pfizer	0.89%
Lockheed Martin	0.79%

Largest Underweights

Verizon Comms	(0.69%)
Google	(0.55%)
Procter & Gamble	(0.50%)
Walt Disney	(0.49%)
Sanofi	(0.45%)

* Measured against MSCI World ex UK (NDR)

Top 10 Holdings

1	Apple Inc	£7,941,629	6	General Electric Co	£3,892,290
2	Microsoft Corp	£6,359,969	7	Archer-Daniels	£3,858,905
3	Pfizer Inc	£5,214,856	8	Citigroup Inc	£3,775,062
4	JPMorgan Chase	£5,139,063	9	Northrop Grumman	£3,771,762
5	Exxon Mobil Corp	£4,473,859	10	Oracle Corp	£3,717,636

Hymans Robertson View

There was no significant business news from Invesco over the period. Hymans have a slight reservation about the complexity / lack of transparency of the strategy but they still think there is a high probability they will meet their objectives.

Risk Control

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

**Lincolnshire Pension Fund
Global Equities – Neptune
Quarterly Report September 2014**

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.

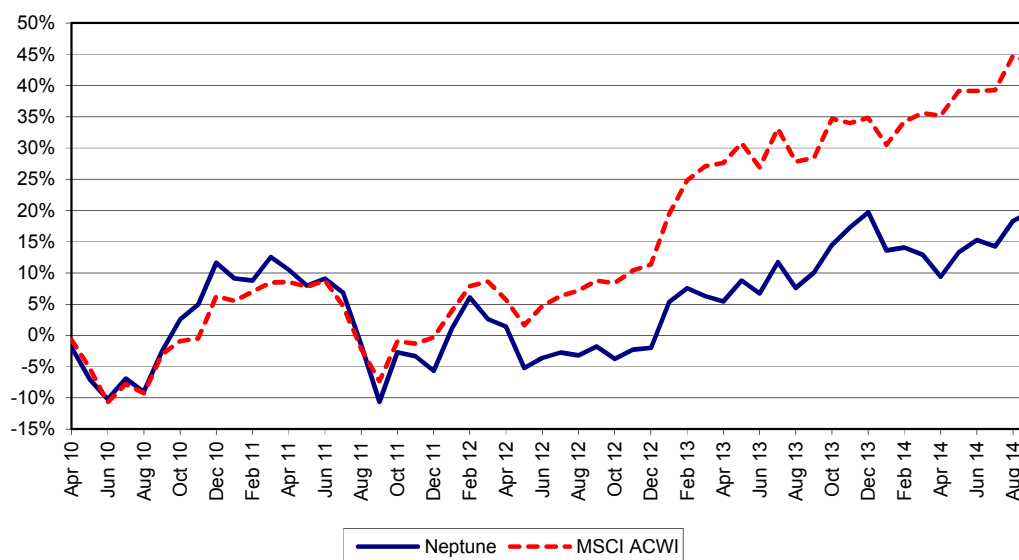
Portfolio Valuation

Value at 30.06.14	Value at 30.09.14
£80,183,778	£83,608,504

Performance

The portfolio returned 4% in the quarter and outperformed the index by 0.8%. The Fund's main overweights were in industrials, information technology and financials. There was notable strength in the information technology sector, especially from Facebook, Apple and Baidu. US financial institutions that the Fund held were also strong positive contributors, although exposure to Japanese property firms was a detractor as they lacked the asset reflationary catalyst of renewed QE. Japanese exposure greatly helped Neptune's continued hedging of yen exposures back into sterling. There was, however, some weakness in Neptune's European holdings, notably the auto manufacturers.

Neptune Performance Since Inception



	Quarter %	1 Year %	3 Year %	5 Year %	Inception* %
Neptune	4.0	8.9	10.3	n/a	4.1
MSCI ACWI**	3.2	11.8	15.7	n/a	8.4
Relative Performance	0.8	(2.6)	(4.7)	n/a	(3.9)

* annualised, inception date 16/04/2010

Turnover

Holdings at 30.06.14	Holdings at 30.09.14	Turnover in Quarter %	Turnover in Previous Quarter %
51	47	25.2	25.4

Purchases and Sales

Portfolio transactions undertaken during the quarter did not represent a change in strategy but rather stock-specific switches within sectors (such as selling Sumitomo Mitsui Financial Group for Daiwa Securities) and adding new names, notably within Japanese industrials. The only exception to that was a retrenchment away from Europe, where Neptune sold the underperforming auto stocks, reflecting the risks posed by uncertainty around the ECB's monetary policy versus our confidence elsewhere in the world, notably the US and Japan. Neptune also increased their weighting to India by adding a holding in the Neptune India Fund. This is in addition to the two stocks they bought in India in the second quarter, and offers broader exposure to the market than the direct holdings in ICICI Bank and Larsen & Toubro.

Top 5 Contributions to Return

Facebook Inc	0.7%
Baidu.Com Spon ADR	0.7%
CME Group Inc	0.6%
Morgan Stanley	0.5%
Apple Computer Inc	0.4%

Bottom 5 Contributions to Return

Yum Brands Inc	(0.4%)
Sberbank-Spon ADR	(0.4%)
AGCO Corp	(0.3%)
Daimler Chrysler AG	(0.2%)
Kajima Corp	(0.2%)

Top 10 Holdings

1	CME Group Inc	£3,205,595
2	Facebook Inc	£3,169,108
3	Baidu Inc - ADR	£2,961,244
4	Fanuc Corp	£2,910,949
5	Taisei Corp	£2,876,310

6	Komatsu Ltd	£2,665,788
7	Mitsui Fudosan	£2,649,916
8	Apple Inc	£2,609,925
9	Marsh & Mclennan Cos	£2,582,858
10	Google Inc	£2,541,227

Hymans Robertson View

There was no significant business news from Neptune over the period. Hymans remain unconvinced that Neptune is able to sustain performance following the success of its high allocation to emerging markets in its formative years and they note that assets under management are reducing despite a wide range of investment strategies. Hymans rating remains at 2 – Sell, review options.

Hymans will be meeting with Neptune in early 2015 to gain a better understanding of the investment process that Neptune follows.

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 2014**

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.

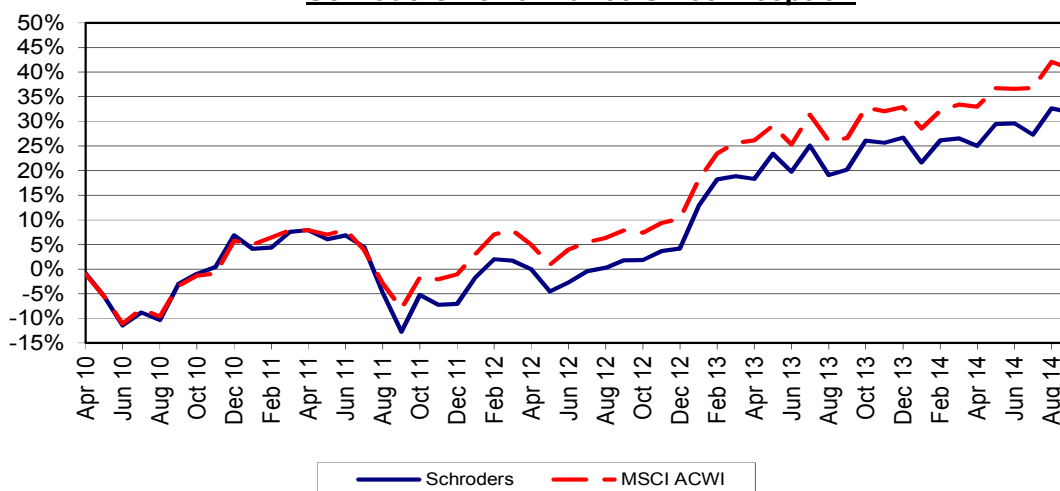
Portfolio Valuation

Value at 30.06.14	Value at 30.09.14
£86,622,173	£88,121,764

Performance

The portfolio underperformed the benchmark over the period despite a positive contribution from stock selection across all regions with the exception of North America. Over all other periods Schroders continue to underperform against their benchmark.

Schroders Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Schroders	1.8	9.7	14.8	n/a	6.3
MSCI ACWI (Net)	3.0	11.2	15.3	n/a	7.9
Relative Performance	(1.2)	(1.2)	(0.4)	n/a	(1.44)

*annualised since Inception April 16 2010

Turnover

Holdings at 30.06.14	Holdings at 30.09.14	Turnover in Quarter %	Turnover in Previous Quarter %
67	67	13.4	10.8

Purchases and Sales

Schroder's have added structural winners Reckitt Benckiser and Nestle to the portfolio and opportunistic stocks Marathon Oil and Hilton. Purchases have been funded by sales of names where the growth gap has closed, limiting Schroder's expectations for further upside (TripAdvisor and Universal Health), and those expected to deliver earnings disappointment (Mondelez).

Top 5 Contributions to Return

Amgen	0.6%
Nokia	0.3%
Kasikombank	0.3%
Citigroup	0.2%
ebay	0.2%

Bottom 5 Contributions to Return

Walgreen	(0.4%)
Heidelbergcement	(0.3%)
Harley-Davidson	(0.3%)
Schneider Electric	(0.3%)
Schlumberger	(0.3%)

Top 10 Holdings

1	Amgen	£2,937,171	6	Google	£2,090,704
2	Citigroup	£2,247,137	7	Nokia	£1,865,678
3	Schlumberger	£2,222,844	8	JPMorgan Chase	£1,765,043
4	Roche Holding	£2,176,292	9	Danaher Corp	£1,759,812
5	SMC	£2,112,431	10	Harley-Davidson	£1,758,224

Hymans Robertson View

The Schroder Global Equity team comprises 13 individuals including Alex Tedder (recently recruited from American Century), Simon Webber and Sue Chan, 8 Global Sectors Specialists ("GSS") and 2 product managers. Tedder indicated that he had implemented a reorganisation which might lead to some changes in team composition. Since the period end Hymans have seen some activity with former lead manager, Virginie Maisonneuve, recruiting 2 GSS's, Giles Money and Lucretia Tam to her new employer, PIMCO. Schroder believes that this is the extent of Maisonneuve's recruitment drive. Schroder may undertake its own recruitment activity in due course and in the meantime another GSS, James Gautrey, has been promoted to portfolio manager. Hyman's view is that the team can absorb the loss of Money and Tam but they are retaining their 'On Watch' rating until there is more clarity on Tedder's initiatives and the long run composition 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 – Threadneedle
Quarterly Report September 2014**

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.

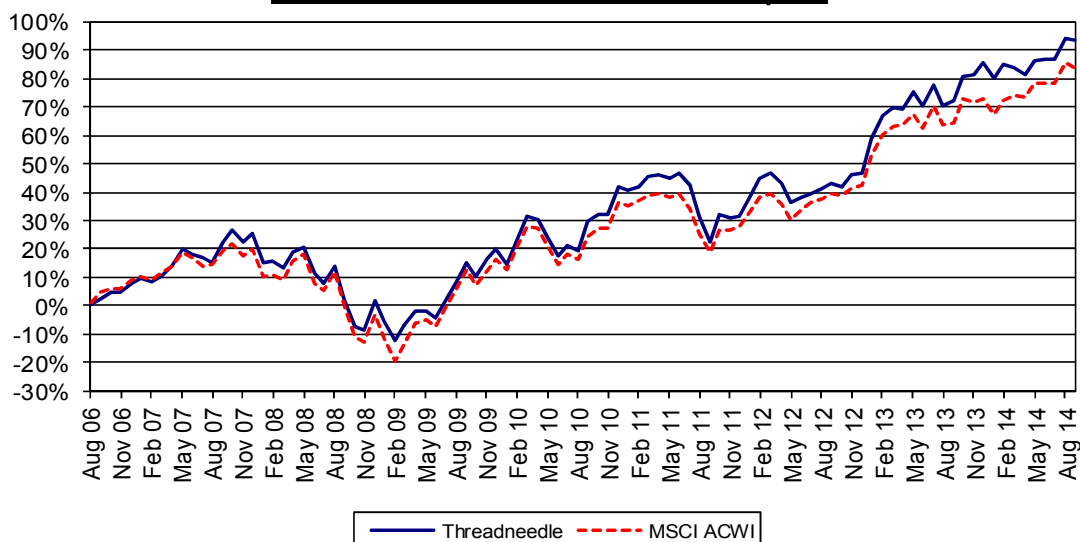
Portfolio Valuation

Value at 30.06.14	Value at 30.09.14
£89,614,986	£92,629,923

Performance

The fund outperformed its benchmark in the third quarter. Regional positioning was favourable, as the US, where Threadneedle are overweight, outperformed Europe and the Far East, where they are underweight. At the stock level, strong performance by their selections in consumer discretionary, healthcare and materials led to a positive return overall.

Threadneedle Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Threadneedle	3.4	12.1	16.4	10.9	8.4
MSCI ACWI	3.2	11.8	15.7	10.3	7.7
Relative Performance	0.2	0.3	0.6	0.5	0.6

* annualised, inception date 01/08/2006

Turnover

Holdings at 30.06.14	Holdings at 30.09.14	Turnover in Quarter %	Turnover in Previous Quarter %
94	93	10.2	19.8

Purchases and Sales

Threadneedle added to an existing position in methanol producer Methanex and opened new positions in car rental firm Hertz and Vertex Pharmaceuticals. They sold semiconductor firm Lam Research, the sector has performed well, and they now think Applied Materials, which they purchased recently, offers more upside as a merger with Tokyo Electron is worked through.

Top 5 Contributions to Return

Gilead Sciences	0.8%
Apple	0.4%
Bank of Ireland	0.3%
Facebook	0.3%
Amgen	0.2%

Bottom 5 Contributions to Return

Copa Holdings	(0.3%)
Suncor Energy	(0.2%)
Continental	(0.2%)
Nomura Holdings	(0.2%)
Samsung Electronics	(0.2%)

Top 10 Holdings

1	Apple Inc	£2,462,899
2	Mazda Motor Corp	£1,967,139
3	Gilead Sciences	£1,885,718
4	Methanex Corp	£1,865,042
5	Disney (Walt) Com	£1,813,056

6	Sekisui Chemical	£1,769,715
7	Union Pacific Corp	£1,755,351
8	Anheuser-Busch	£1,746,584
9	Nestle SA	£1,737,814
10	Suncor Energy	£1,715,130

Hymans Robertson View

In September, Threadneedle announced that its Head of UK Equities, Simon Brazier and co-manager Blake Hutchins along with two European analysts and an investment specialist, were leaving to join Investec. Threadneedle's UK equity desk manages some £18bn of assets. The team will still comprise 9 investment professionals after these departures. Leigh Harrison led the team from 2006 – 2011 before taking on the role of Head of Equities. He continued to run some money directly and will expand that responsibility as well as re-assuming his previous position as Head of UK Equities. It is disappointing to record further changes in the UK team; only 4 team members, including Harrison, have been with the UK team for over 5 years. Hymans are optimistic that the global equity team is now more settled under William Davis but staff turnover in the wider firm is still higher than they would like. Hymans continue to rate the strategy at 4 – Retain.

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 2014**

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 30.06.14	Value at 30.09.14
£76,514,346	£78,896,781

Performance

During the quarter the fund returned 3.1% marginally lagging the index which returned 3.2%. In the quarter stock selection in consumer staples and the portfolio's underweight in healthcare were negative contributors. The zero weight in energy and materials, stock selection and allocation to consumer discretionary and industrials, stock selection in financials, zero weight in utilities and allocation to information technology were positive contributors.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	3.1	9.2	N/A	N/A	13.3
MSCI World Index	3.2	12.1	N/A	N/A	18.3
Relative Performance	(0.1)	(2.6)	N/A	N/A	(4.2)

*annualised, inception date 18/06/2012

Purchases and Sales

During the quarter Morgan Stanley bought Japan Tobacco and added to their positions in Diageo and Publicis. They reduced their positions in Swedish Match, Kraft, Moody's and Time Warner.

Top 3 Contributions to Return

Microsoft	0.8%
Sanofi	0.7%
Procter & Gamble	0.6%

Bottom 3 Contribution to Return

LVMH	(0.3%)
Publicis	(0.2%)
Mondelez	(0.1%)

Top Ten Holdings

Company	Industry	% Weighting
British American Tobacco	Tobacco	9.3
Nestle	Food Products	8.9
Unilever	Food Products	7.6
Reckitt Benckiser	Household Products	7.1
Sanofi-Aventis	Pharmaceuticals	6.0
Procter & Gamble	Household Products	4.9
Microsoft	Software	4.9
Diageo	Beverages	4.7
Accenture	IT Services	4.7
Philip Morris	Tobacco	4.6

Hymans Robertson View

There was no significant business news from Morgan Stanley over the period. The Global Brands strategy has moderately reduced exposure to its core consumer staples holdings which have underperformed over the last year or so but has otherwise retained its defensive profile. The newly launched sister strategy, Global Quality, has fared slightly better over its first 12 months but it is far too early to draw any conclusions from that. Global Quality has grown steadily to assets of £1.3bn over that period. Global Brands has assets of c.£9.5bn and remains closed to segregated accounts though new clients for the pooled fund are considered on a case by case basis. At this stage Hymans do not see capacity across the two strategies as a problem and retain their rating on Global Brands at 5 – Preferred strategy.

**Lincolnshire Pension Fund
Passive Bonds – Blackrock
Quarterly Report September 2014**

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 June 2014

Portfolio	30.06.14 £	30.09.14 £
Corporate Bond All Stocks Index Fund	50,369,749	51,833,986
Over 5 Years UK Index-Linked Gilt Index Fund	29,959,128	31,735,392
Overseas Bond Index Fund	18,902,402	19,256,038
Total	99,231,279	102,825,416

Performance

Over all periods the portfolio has matched the benchmark.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock	3.6	6.7	6.0	n/a	6.8
Composite Benchmark	3.6	6.7	6.0	n/a	6.7
Relative Performance	0.0	0.0	0.0	n/a	0.0

*annualised since inception 28/07/10

Hymans Robertson View

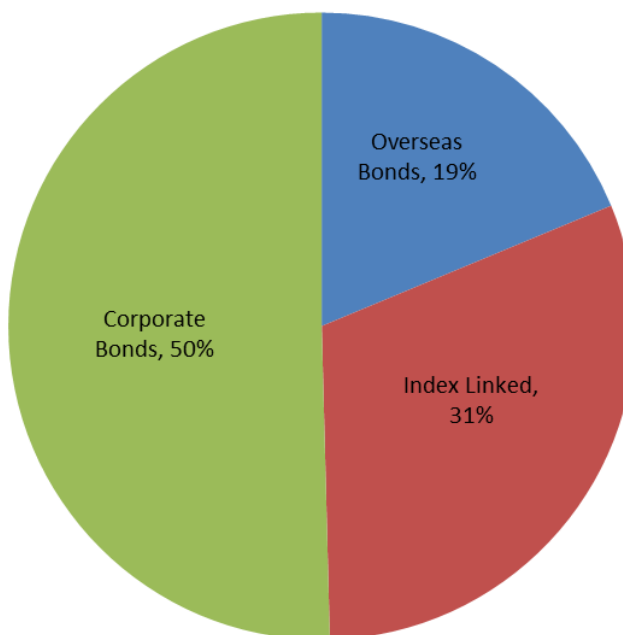
There were no significant developments within the Index Fixed Income team over the quarter; as such Hymans continue to rate Blackrock as one of their preferred passive fixed income managers.

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 2014



**Lincolnshire Pension Fund
Absolute Return Bonds – F&C
Quarterly Report September 2014**

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 30.06.14	Value at 30.09.14
£102,127,622	£99,549,520

Performance

During the quarter the fund fell by 2.5% and underperformed the target return by 3.4%. All three strategies in the portfolio generated a negative return over the quarter. F&C are not concerned that the portfolio construction is amplifying similar bets and they remain happy with the overall portfolio, in spite of a few disappointing months. The overall credit quality of the portfolio remains good, and F&C are comfortable with the exposures within the Fund.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
F&C	(2.5)	2.4	2.7	n/a	2.2
3 Month LIBOR + 3%	0.9	3.6	3.7	n/a	3.8
Relative Performance	(3.4)	(1.1)	(1.0)	n/a	(1.5)

* 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:

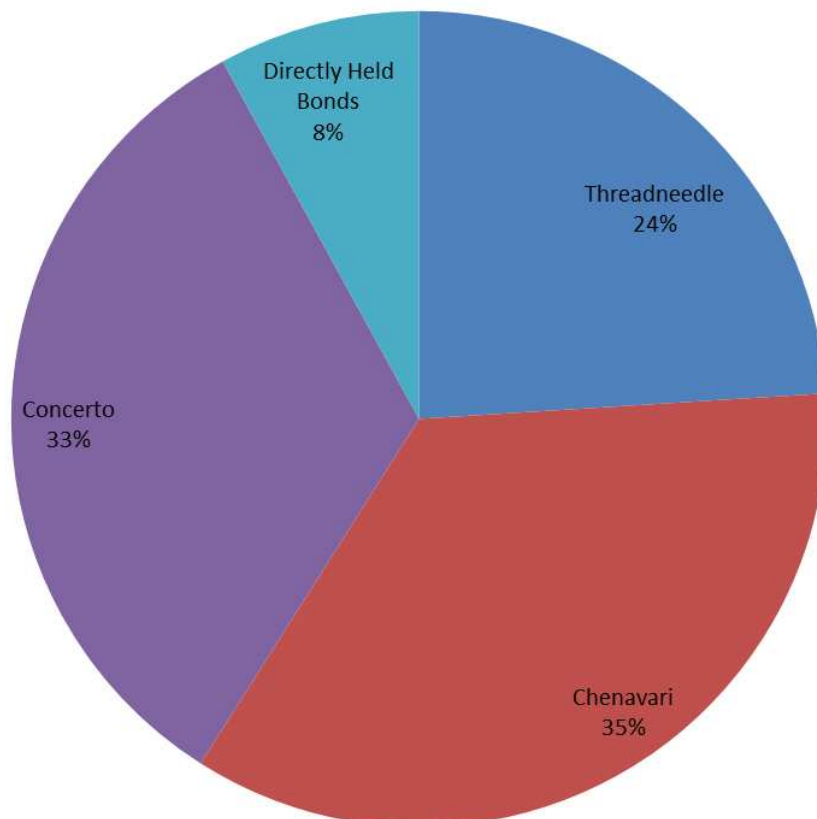
Threadneedle	Interest rates, currency
Chenavari	Credit
Concerto	Credit

Hymans Robertson View

As Hymans indicated in the Q2 report, there has been little change to the management of the Absolute Return Fund due to the new ownership of F&C by Bank of Montreal (BMO). Ben Fox continues to manage the Fund, and is supported by a significant team of macro, quant and multi strategy specialists. Hymans had a research meeting with Fox in September 2014 which raised no concerns over the

management of the Fund, or F&C's continued commitment to the Fund, despite the other large investor liquidating their holding. Two future developments which were discussed included potentially increasing the existing return target for the Fund and re-branding the Fund under the F&C banner. Hymans maintain their "4 –Retain" rating but will continue to monitor the manager closely.

The pie chart below shows the allocation as at 30th September 2014



**Lincolnshire Pension Fund
Alternative Investments – Morgan Stanley
Quarterly Report September 2014**

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 30.06.14	Value at 30.09.14
£143,833,989	£154,652,811

Performance

The portfolio declined 0.6% during the third quarter. Manager selection was the largest driver of returns while strategic allocation modestly detracted. Tactical decisions were additive to relative returns.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	(0.6)	5.4	7.3	n/a	5.8
3 Month LIBOR + 4%	1.2	4.6	4.8	n/a	4.8
Relative Performance	(1.7)	0.8	2.4	n/a	0.9

* 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.

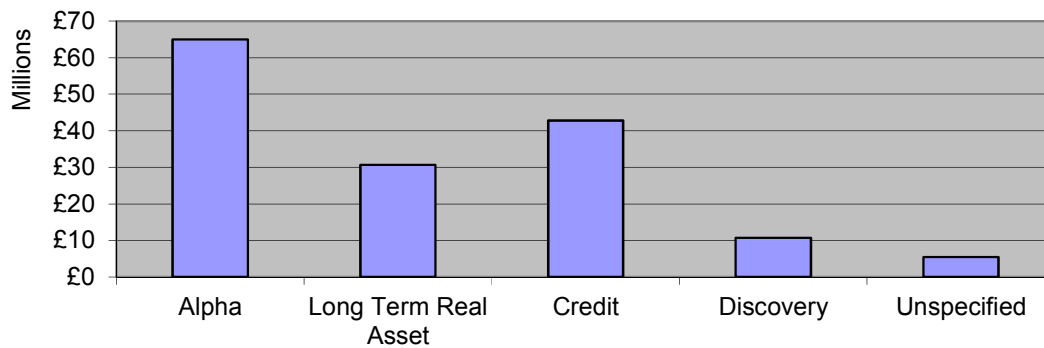
Long Term Real Asset – These are long term investments that seek to access illiquidity premium. Investments include Private Equity, Infrastructure, Real Estate, Commodities and Inflation – linked strategies.

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 30th September 2014



Portfolio Positioning

During the quarter, Morgan Stanley continued to moderate their overall exposure to credit through reductions in high yield and EM debt. Additionally, they reduced their exposure to interest rate sensitive assets in light of the potential for interest rates increases and broadened their exposure to hedge funds to include more alpha and opportunistic strategies. Morgan Stanley also initiated positions in private renewable energy infrastructure. They also committed to a specialist European manager which focuses on onshore wind, solar photovoltaic (PV) and biomass and have a second commitment to a niche UK solar PV opportunity.

Hymans Robertson View

Morgan Stanley remain one of their favoured managers for diversified alternatives mandates and this team now manage £2.7bn across its segregated portfolios and pooled fund. This portfolio offers exposure to a broad range of alternative assets that typically offer diversification from traditional asset classes, equities, fixed income and bonds. Morgan Stanley adopts a typical multi-asset framework and over the long-term the portfolio is expected to generate 50% of performance from the strategic asset allocation, 25% from manager selection and 25% from medium-term asset allocation. Morgan Stanley employs an open architecture approach, investing through both internal and external fund managers. The team responsible for this portfolio has been highly stable and the three portfolio managers, Joe McDonnell in London, Ryan Meredith and Rui de Figueiredo in New York, have many years' experience in the management of alternative investments. Hedge Funds continue to be a core strategic allocation within the portfolio due to what Morgan Stanley believes to be their attractive characteristics. Manager selection is critical to success when investing in hedge funds and Morgan Stanley therefore gains exposure through investing in its own in-house multi-strategy fund of hedge fund which currently represents approximately 25% of the portfolio.

Risk Control

Portfolio volatility since inception is 3.99% within the guidelines specified by the mandate.

Conclusion

Over the quarter the Fund has produced a positive return of 1.77% which is slightly behind the benchmark. Managers have had mixed returns with six of the nine managers producing a positive return.

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.

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