Lincolnshire
COUNTY COUNCIL
Working for a better future

Regulatory and Other Committee

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

Report to:	**Pensions Committee**
Date:	**09 April 2015**
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 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

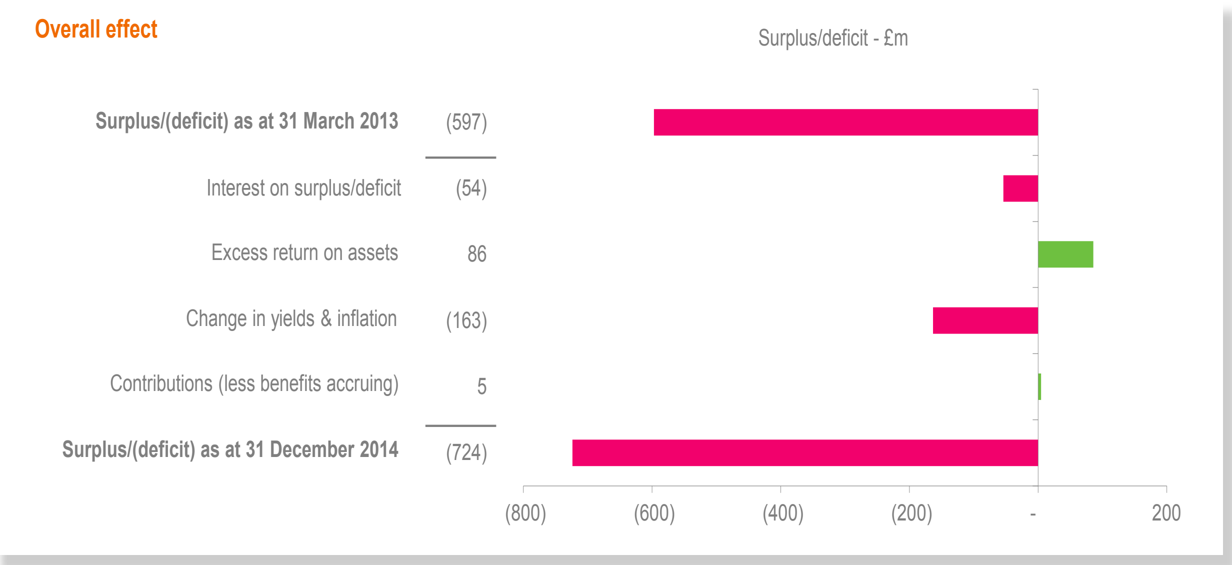
1.1 The funding update is provided to illustrate the estimated development of the funding position from 31st March 2013 to 31st December 2014, for the Fund.

1.2 As the graph below shows, the funding level at the latest formal valuation was 71.5%. As at 31st December 2014 the funding level has decreased to 70%.

Change in funding level since last valuation

1.3 As shown below, the deficit in real money has increased from £597m to £724m between the period 31st March 2013 and 31st December 2014. This has been a result of the change in bond yields and interest on the deficit, however this has been slightly offset by the excess return on assets achieved by the Fund.

What's happened since last valuation?



1.4 In the period since 30th September 2014, the funding level has fallen from 73.8% to 70% as a result of the recent fall in government bond yields and the deficit was £582m.

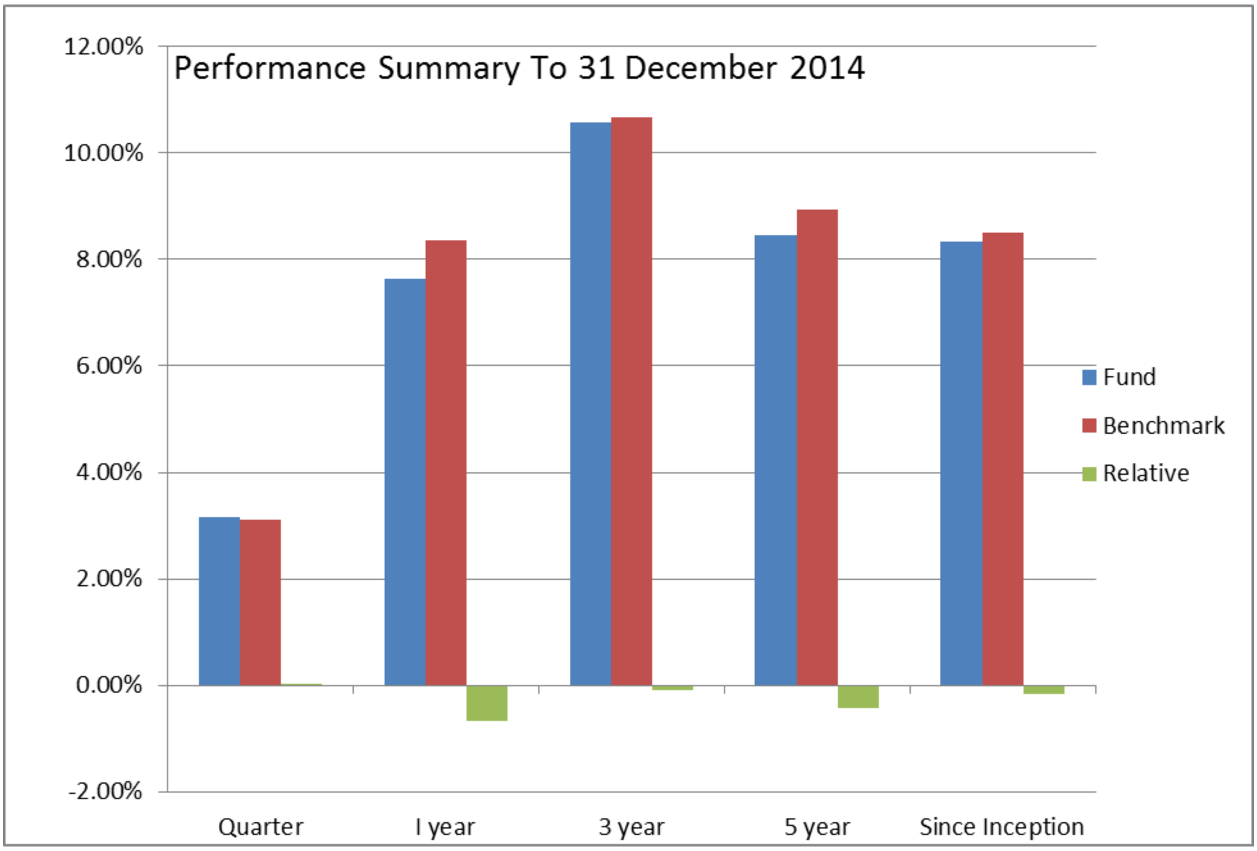
2. Fund Performance & Asset Allocation

2.1 The Fund increased in value by £22.8m during the quarter from £1,647m to £1,669.8m, 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	Q4 2014 £	Q3 2014 £	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	314.8	318.9	18.9	20.0	(1.1)
Global Equities	719.1	690.7	43.0	40.0	3.0
Alternatives	236.3	235.0	14.2	15.0	(0.8)
Property	190.2	185.7	11.4	11.5	(0.1)
Fixed Interest	206.5	202.4	12.3	13.5	(1.2)
Cash	2.8	14.3	0.2	0.0	0.2
Total	**1,669.8**	**1,647.0**	100.0	100.0	

2.2 The graph below shows the Fund's performance against the benchmark over the quarter, one year, three years, five years and since inception. The Fund has a target to outperform the strategic benchmark by 1% per annum.

2.3 Over the quarter, the Fund produced a positive return of 3.16% outperforming the benchmark which returned 3.12%. The Fund is behind the benchmark over all other 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 one change to the ratings during the quarter. Hymans Robertson met with Neptune to gain a better understanding of their investment process, following this meeting Hymans have changed their rating from "strongly on watch" to "on watch". Sixteen managers remained rated as retain and four managers, Rreef Property Ventures Fund 3, Aviva Pooled Property Fund, Neptune and Schroders, as "on watch". Officers will monitor these managers closely and arrange meetings to discuss any potential issues

3.3

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 seven of the nine managers producing a positive absolute return. Over the quarter, five managers outperformed their benchmark, whilst Invesco and the in house team slightly underperformed by 0.2% and F&C and Morgan Stanley disappointed underperforming by 2.5% and 2.2%. Over the 12 month period only F&C have failed to produce a positive absolute return. Against their target, the in house team, Invesco, Morgan Stanley Global Brands and Blackrock have beaten the required return.

	3 months ended 31/12/14			Previous 12 months			
Manager	Manager Return %	Index Return %	Relative Variance %	Manager Return %	Index Return %	Relative Variance %	Target p.a. %
Passive UK Equity In house	0.0	0.3	(0.2)	0.5	0.4	0.1	+/- 0.5
Invesco (Global Equities (ex UK))	5.3	5.5	(0.2)	13.3	12.5	0.7	+1.0
Threadneedle (Global Equities)	4.9	4.5	0.4	9.3	11.2	(1.7)	+2.0
Neptune (Global Equities)	6.7	4.5	2.1	6.8	11.3	(4.0)	+4.0
Schroder's (Global Equities)	5.7	4.4	1.2	10.0	10.7	(0.6)	+3.0
Morgan Stanley Global Brands	6.0	5.0	0.9	11.9	11.5	0.4	n/a
Blackrock (Fixed Interest)	5.6	5.4	0.2	13.8	13.6	0.2	Match Index
F&C (Fixed Interest)	(1.7)	0.9	(2.5)	(1.3)	3.6	(4.8)	3M LIBOR + 3%
Morgan Stanley (Alternative Investments)	(1.1)	1.2	(2.2)	1.9	4.7	(2.6)	3M LIBOR + 4%

Lincolnshire Pension Fund
UK Equities – In House (Passive UK)
Quarterly Report December 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.

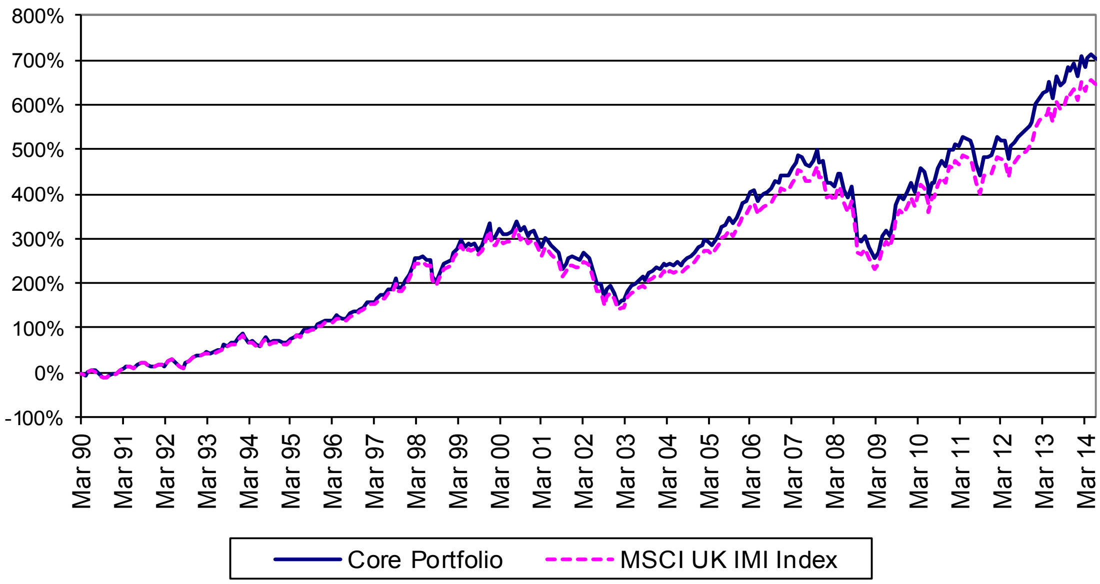
Portfolio Valuation

Value at 30.09.14	Value at 31.12.14
£318,884,035	£314,780,654

Performance

During the quarter the portfolio underperformed the index by 0.2%. This was due to underweight positioning in the consumer discretionary and financial sectors which both produced positive returns in the quarter. The portfolio was also overweight energy which produced a negative return during the quarter. 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	0.0	0.5	10.7	8.7	8.6
MSCI UK IMI	0.3	0.4	10.7	8.6	8.3
Relative Performance	(0.2)	0.1	0.0	0.1	0.3

* annualised, inception date 01/10/1989

Turnover

Holdings at 30.09.14	Holdings at 31.12.14	Turnover in Quarter %	Turnover in Previous Quarter %
249	248	0.01	0.1

Purchases and Sales

During the quarter the manager increased positions in Lloyds, RBS, Barclays and Jupiter which reduced the underweight position in financials. The manager also took new positions in Merlin Entertainment and Intu Properties and increased the holding in Tui following the merger with Tui Germany.

Largest Overweights

Babcock Intl	0.12%
Royal Dutch Shell	0.10%
British American Tobacco	0.09%
BG Group	0.07%
Standard Chartered	0.10%

Largest Underweights

Londonmetric	(0.05%)
Kier Group	(0.05%)
SVG Capital	(0.05%)
Crest Nicholson	(0.05%)
Workspace Group	(0.05%)

* Measured against MSCI UK IMI

Top 10 Holdings

1	Royal Dutch Shell	£22,965,266
2	HSBC Holdings	£18,984,169
3	BP	£12,738,060
4	GlaxoSmithkline	£11,457,051
5	British American Tobacco	£11,148,935

6	Vodafone Group	£10,329,125
7	Astrazeneca	£9,120,111
8	Diageo	£7,728,652
9	Rio Tinto	£6,564,841
10	Lloyds Banking Group	£6,536,338

Risk Control

The portfolio has a tracking error limit of 0.5%. At the end of December 2014 the tracking error was 0.24%.

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

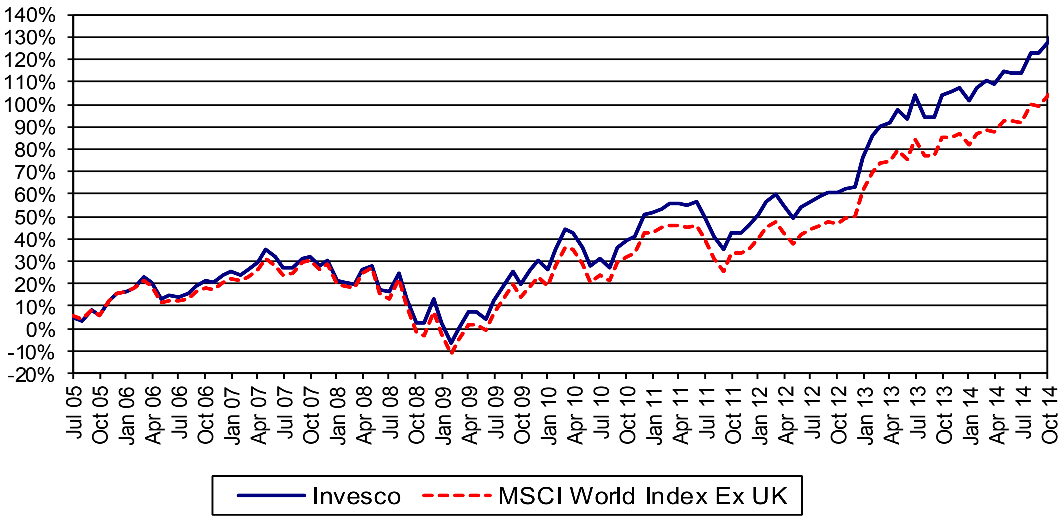
Portfolio Valuation

Value at 30.09.14	Value at 31.12.14
£347,438,525	£355,830,048

Performance

During the quarter Invesco's strategy underperformed its benchmark. Stock Selection had a negative impact on relative performance. Intended overweights in stocks with a high earnings expectations score and strong market sentiment added to performance, while stocks with a high value score detracted from performance. An underweight position in Healthcare helped performance, whilst being underweight Materials detracted from performance. Contributions from Countries and Currencies were negative. Overweights in Danish stocks and underweights in US stocks hurt performance.

Invesco Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Invesco	5.3	13.3	17.2	12.5	9.4
MSCI World ex UK	5.5	12.5	15.9	11.3	8.2
Relative Performance	(0.2)	0.7	1.1	1.1	1.2

* annualised, inception date 1st July 2005

Turnover

Holdings at 30.09.14	Holdings at 31.12.14	Turnover in Quarter %	Turnover in Previous Quarter %
417	429	8.0	7.5

Purchases and Sales

During the quarter Invesco added Canadian Tire, Morgan Stanley and Heineken and increased positions in Hess and Western Union. These were funded by selling Liberty Ventures and Tyson Foods and decreasing positions in Anheuser-Busch, Macy's and Mckesson.

Largest Overweights

Northrop Grumman	1.01%
Archer Daniels	0.93%
Pfizer	0.88%
Nippon Tel & Tel	0.77%
Edison	0.72%

Largest Underweights

Verizon Comms	(0.64%)
Procter & Gamble	(0.53%)
Walt Disney	(0.51%)
Google	(0.50%)
Visa	(0.43%)

* Measured against MSCI World ex UK (NDR)

Top 10 Holdings

1	Apple Inc	£8,317,877
2	Microsoft Corp	£6,223,123
3	Pfizer Inc	£5,359,978
4	JPMorgan Chase	£5,210,314
5	Exxon Mobil Corp	£4,291,763
6	Oracle Corp	£4,259,785
7	Johnson & Johnson	£3,963,500
8	Northrop Grumman	£3,892,895
9	Citigroup Inc	£3,845,757
10	General Electric Co	£3,746,705

Hymans Robertson View

There was no significant business news from Invesco over the period.

Risk Control

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

Lincolnshire Pension Fund
Global Equities – Neptune
Quarterly Report December 2014

Investment Process

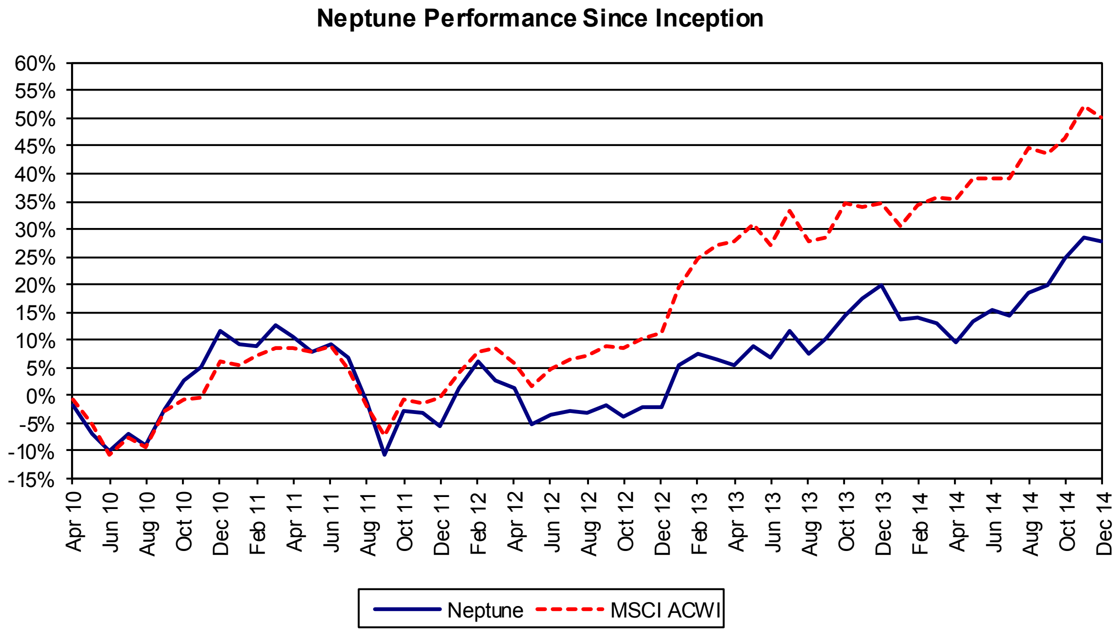
This portfolio is mandated to outperform the MSCI All Countries World Index by 2% to 4% over rolling three year periods, net of fees. This is achieved through generating capital growth from a concentrated portfolio of global securities, selected from across world equity markets. The investment process of Neptune means that they will usually generate more volatile returns that the Fund's other Global Equity Managers and are seen as benchmark agnostic.

Portfolio Valuation

Value at 30.09.14	Value at 31.12.14
£83,608,504	£89,349,824

Performance

During the quarter produced a positive return of 6.7% against the benchmark of 4.5%. The macro environment benefitted the Fund, which had its largest absolute weighting the US. Neptune's technology exposure continued to benefit the Fund, particularly Apple and LinkedIn, whilst Neptune's US financials holdings all contributed positively to relative performance. Neptune also continued to profit from their high conviction overweight in Japan, whilst the Fund's yen hedge boosted performance in a quarter which saw further yen depreciation.



	Quarter %	1 Year %	3 Year %	5 Year %	Inception* %
Neptune	6.7	6.8	10.7	n/a	5.3
MSCI ACWI**	4.5	11.3	14.6	n/a	8.9
Relative Performance	2.1	(4.0)	(3.4)	n/a	(3.3)

* annualised, inception date 16/04/2010

Turnover

Holdings at 30.09.14	Holdings at 31.12.14	Turnover in Quarter %	Turnover in Previous Quarter %
47	46	10.4	25.2

Purchases and Sales

Portfolio activity was limited during the quarter, with Neptune increasing its exposure to Japan through the addition of Isetan Mitsukoshi and Sumitomo Realty and Development. This was funded through the sale of a Chinese consumer stock and a slight reduction in their financials exposure.

Top 5 Contributions to Return

ICICI Bank	0.7%
CME Group	0.7%
Apple Computer Inc	0.5%
Linkedin Corp	0.4%
Honeywell Intl	0.3%

Bottom 5 Contributions to Return

Google Inc	(0.2%)
Isetan Mitsukoshi	(0.2%)
Kajima Corp	(0.2%)
Mitsubishi Heavy Ind	(0.2%)
Mitsui Fudosan	(0.2%)

Top 10 Holdings

1	CME Group Inc	£3,778,900
2	Apple Inc	£3,610,313
3	ICICI Bank	£3,333,333
4	Taisei Corp	£3,197,122
5	Fanuc Corp	£2,879,865
6	Komatsu Ltd	£2,799,628
7	Mitsui Fudosan	£2,784,543
8	Sumitomo Realty	£2,761,823
9	Mitsubishi Estate	£2,732,336
10	Linkedin Corp	£2,724,368

Hymans Robertson View

Hymans have raised their rating on Neptune Global Equity from "2 – Sell, review options‟ to '3 - On Watch' following a recent meeting. They are encouraged by a number of recent intitiatives taken by the manager including: a substantial rationalisation of the product range; a stabilisation in fund outflows; a programme to make some more senior investment hires and a tightening of the investment process to include model portfolios for all global sectors. Nonetheless, Hymans still have meaningful reservations: assets at £4.8bn are quite low given the scale of Neptune's team; despite the longer tenure of a few, key individuals, overall staff retention needs to improve and key man risk with Geffen remains extremely high. During the period Neptune announced the closure of its sub-scale China and Russia Special Situations Funds and closed its Global Long/Short Sector fund following the departure of Ted Alexander who co-managed the Fund with Neptune founder Robin Geffen. Since the period end Neptune has announced that senior UK portfolio manager Scott Maclennan is leaving the firm and will be replaced by an internal promotion, Mark Martin, who has built up a good reputation managing Neptune's mid-cap strategy.

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 2014

Investment Process

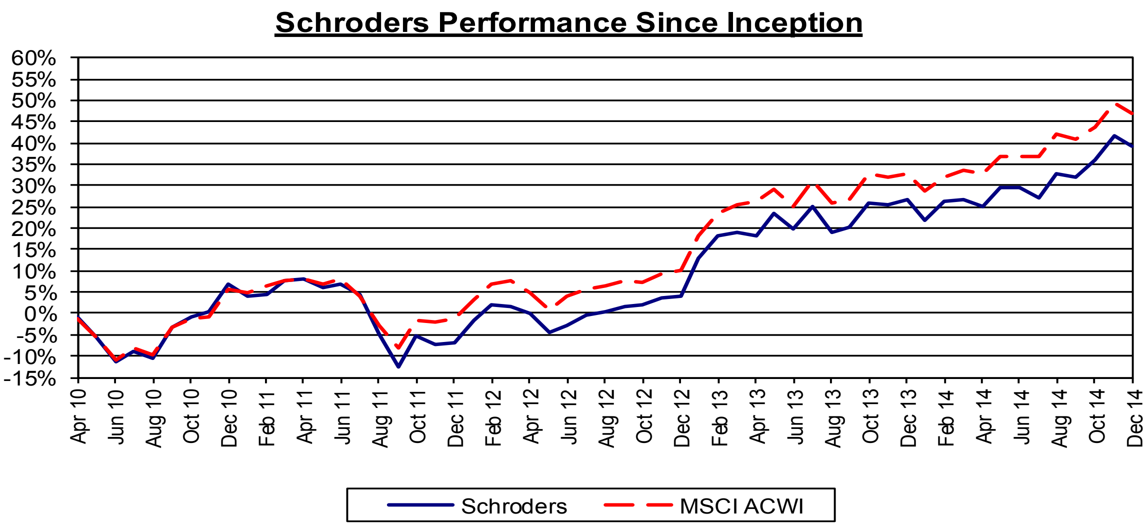
This portfolio is mandated to outperform the MSCI All Countries World Daily Net Index by 2% to 4% over rolling three year periods, gross of fees. This is achieved through an investment approach that is designed to add value relative to the benchmark through both stock selection and asset allocation decisions. 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 30.09.14	Value at 31.12.14
£88,121,764	£93,108,106

Performance

Schroders outperformed the benchmark over the period as their stock selection within the consumer, healthcare and industrials sectors adding the most value. Schroder's stocks in the energy sector proved to be the largest detractor. By region, North America contributed the most, whilst stocks in the UK and emerging markets were also supportive. This was more than enough to offset stock selection in Europe, which was detrimental to performance.



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Schroders	5.7	10.0	14.5	n/a	7.2
MSCI ACWI (Net)	4.4	10.7	14.1	n/a	8.5
Relative Performance	1.2	(0.6)	0.3	n/a	(1.1)

*annualised since Inception April 16 2010

Turnover

Holdings at 30.09.14	Holdings at 31.12.14	Turnover in Quarter %	Turnover in Previous Quarter %
67	67	8.6	13.4

Purchases and Sales

During the quarter Schroders increased their exposure to the consumer sector, in order to take advantage of tailwinds that should support the growth in consumption. New purchases included Wal-Mart and Hershey, both of which should be direct beneficiaries of this trend. These new positions were funded by selling or reducing holdings in Sealed Air, Eaton Corp and BG Group due to the growth gap closing or fundamental risk increasing.

Top 5 Contributions to Return

Walgreen	0.4%
Amgen	0.3%
United Health Group	0.3%
Sensata Technologies	0.3%
Harley-Davidson	0.3%

Bottom 5 Contributions to Return

Statoil	(0.5%)
Marathon Oil	(0.4%)
BG Group	(0.4%)
Schlumberger	(0.3%)
Cemex	(0.3%)

Top 10 Holdings

1	Amgen	£2,780,569
2	Citigroup	£2,440,042
3	Roche Holding	£2,153,387
4	United Health Grp	£2,078,723
5	Harley-Davidson	£2,069,875
6	Danaher Corp	£2,063,162
7	SMC Corp	£2,016,676
8	Google Inc	£1,959,704
9	Taiwan Semiconductor	£1,956,006
10	Wal-Mart Stores Inc	£1,938,277

Hymans Robertson View

Hymans rate Schroders Global Equity at "3 – On Watch". Given the departure of Virginie Maisonneuve to PIMCO and her replacement by Alex Tedder (ex-American Century) along with a number of initiatives from the latter to re-focus the team, Hymans feel a "3" rating is appropriate until a more settled picture emerges. Nonetheless, they are encouraged by the direction Tedder is pursuing. In light of the change in global equity team leadership in 2014, it is perhaps not surprising that the final quarter saw the departure of two of the team's eight Global Sector Specialists. Both Giles Money and Lucretia Tam have left to join Maisonneuve at PIMCO. Whilst this is a reduction in team resource and further departures would certainly be unwelcome, Hymans view this as part of the re-focusing exercise under Tedder's leadership. Hymans would expect the team to be looking to increase resource at some point.

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 2014

Investment Process

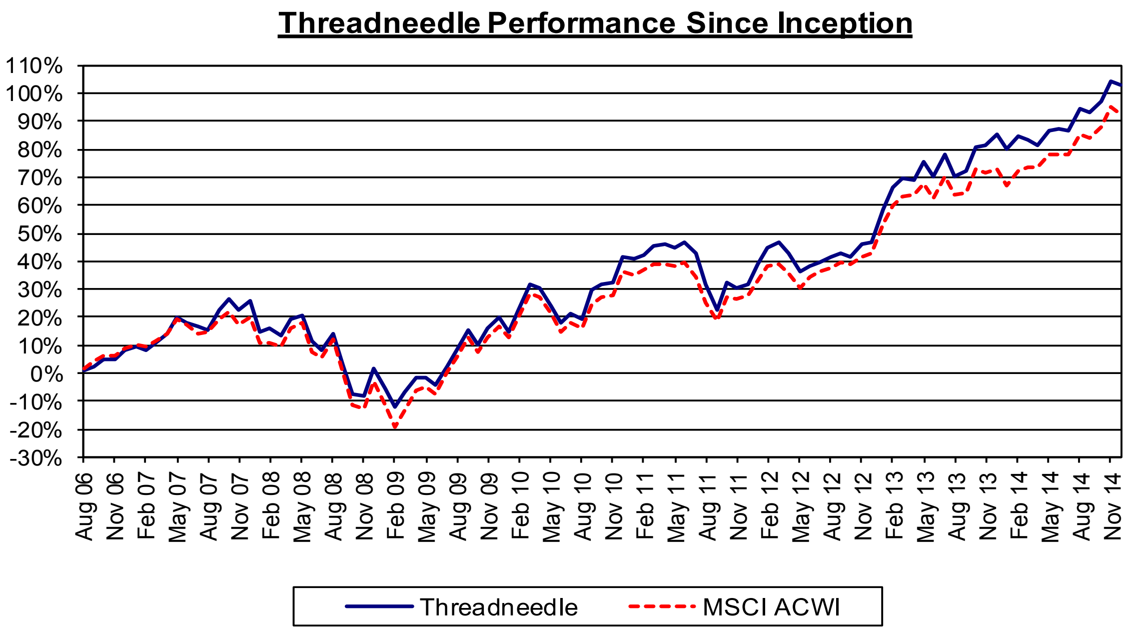
This portfolio is mandated to outperform the MSCI All Countries World Index by 2% per annum, gross of fees over rolling three year periods. This is achieved through investment managers who can draw on their own knowledge and that of other parts of the organisation to implement a thematic approach to stock selection.

Portfolio Valuation

Value at 30.09.14	Value at 31.12.14
£92,629,923	£97,217,115

Performance

Threadneedle outperformed its benchmark in the quarter. Allocation was positive at the regional level, as emerging markets and Europe, where they are underweight, underperformed. Allocation was also positive at the sector level, selection detracted, with energy and materials weighing on returns.



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Threadneedle	4.9	9.3	15.5	11.1	8.8
MSCI ACWI	4.5	11.2	14.6	10.5	8.1
Relative Performance	0.4	(1.7)	0.8	0.5	0.6

* annualised, inception date 01/08/2006

Turnover

Holdings at 30.09.14	Holdings at 31.12.14	Turnover in Quarter %	Turnover in Previous Quarter %
93	87	8.5	10.2

Purchases and Sales

Threadneedle exited United Rentals, Aegon, Blackstone and Suncor during the quarter and added to their holding in Express Scripts. Threadneedle also increased their exposure to financials by purchasing China's Ping An Insurance.

Top 5 Contributions to Return

Ping An Insurance	0.4%
Express Scripts	0.4%
Apple	0.4%
Visa Inc	0.3%
Union Pacific Corp	0.3%

Bottom 5 Contributions to Return

Methanex Corp	(0.6%)
Halliburton Co	(0.6%)
BG Group	(0.3%)
Total SA	(0.3%)
Taiheiyo Cement Co	(0.2%)

Top 10 Holdings

1	Apple Inc	£2,508,389
2	Nestle SA	£2,217,703
3	Express Scripts	£2,112,089
4	Disney (Walt) Com	£2,017,999
5	Union Pacific Corp	£2,003,971

6	Gilead Sciences	£1,977,663
7	Sekisui Chemical	£1,930,180
8	Amphenol Corp	£1,898,243
9	Wolseley plc	£1,847,018
10	Anheuser Busch	£1,846,631

Hymans Robertson View

In January 2015 Threadneedle announced that it is to rebrand as “Columbia Threadneedle Investments”. Threadneedle and Columbia are both owned by US quoted Ameriprise Financial. Columbia manages assets of $358bn, largely US based investments for US based clients. Threadneedle manages more internationally based investments of $147bn albeit largely for UK clients. Combined assets will be $505bn (£316bn). This is not a full merger. Both firms will retain separate legal and regulatory identities, there will be no change to existing funds and no redundancies. It is hoped that Columbia Threadneedle will benefit from greater sharing of information and ideas and broader distribution channels. Hymans have not changed any Threadneedle ratings as a result of the rebranding announcement.

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 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.

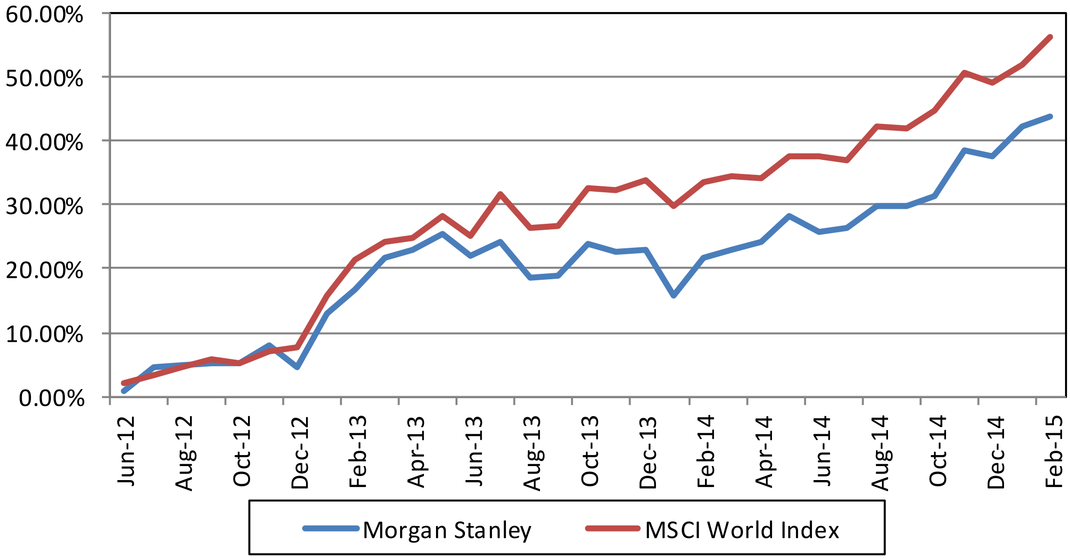
Portfolio Valuation

Value at 30.09.14	Value at 31.12.14
£78,896,781	£83,622,490

Performance

During the quarter Morgan Stanley Global Brands returned 6% outperforming its benchmark by 0.9%. The outperformance for the quarter was primarily due to the zero allocation to Energy. In the quarter stock selection in Information Technology, Consumer Discretionary and Industrials also contributed positively to performance.

Morgan Stanley Global Brands Performance Since Inception



	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley Global Brands	6.0	11.9	N/A	N/A	13.1
MSCI World Index	5.0	11.5	N/A	N/A	16.7
Relative Performance	0.9	0.4	N/A	N/A	(3.1)

*annualised, inception date 18/06/2012

Purchases and Sales

During the quarter Morgan Stanley bought three names, all in the consumer discretionary sector; Walt Disney, 21st Century Fox and Reed Elsevier. They sold out of Swedish Match which was suffering from a more competitive environment and Kraft for valuation reasons, particularly given slow growth prospects in packaged food.

Top 3 Contributions to Return

Visa	1.0%
Time Warner	0.7%
Accenture	0.7%

Bottom 3 Contribution to Return

Sanofi	(1.0%)
Japan Tobacco	(0.1%)
Davide Campari	(0.1%)

Top Ten Holdings

Company	Industry	% Weighting
Nestle	Food Products	9.8
British American Tobacco	Tobacco	9.3
Unilever	Food Products	6.8
Reckitt Benckiser	Household Products	6.6
Microsoft	Software	5.0
Accenture	IT Services	4.8
Procter & Gamble	Household Products	4.8
Time Warner	Media	4.7
Diageo	Beverages	4.6
Philip Morris	Tobacco	4.3

Hymans Robertson View

There was no significant business news from Morgan Stanley over the period. 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 December 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 31st December 2014

Portfolio	**30.09.14 £**	**31.12.14 £**
Corporate Bond All Stocks Index Fund	51,833,986	54,038,112
Over 5 Years UK Index-Linked Gilt Index Fund	31,735,392	33,150,635
Overseas Bond Index Fund	19,256,038	21,402,944
Total	**102,825,416**	**108,591,691**

Performance

Over all periods the portfolio has slightly outperformed the benchmark.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Blackrock	5.6	13.8	6.2	n/a	7.8
Composite Benchmark	5.4	13.6	6.1	n/a	7.7
Relative Performance	0.2	0.2	0.1	n/a	0.1

*annualised since inception 28/07/10

Hymans Robertson View

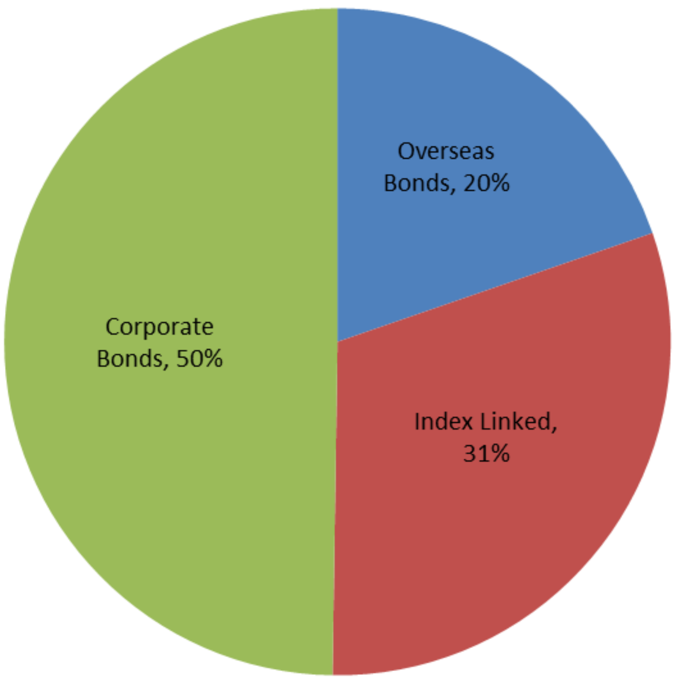
There were no significant developments within the Index Fixed Income team over the quarter; as such Hymans continue to rate Blackrock as one of their preferred passive fixed income managers.

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 2014



Lincolnshire Pension Fund
Absolute Return Bonds – F&C
Quarterly Report December 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 30.09.14	Value at 31.12.14
£99,549,520	£97,880,872

Performance

F&C produced a negative return of 1.7% during the quarter which was 2.5% behind target. The underperformance came largely from F&C's US high yield portfolio run by Concerto, with more moderate returns from the other two portfolios cancelling each other out. Concerto suffered the overspill of plummeting oil prices into the broader high yield market. As well as having direct exposure to the energy sector, performance was further affected by contagion into other sectors, especially within cash markets. While the underperformance was disappointing, F&C expect it to revert somewhat because the credit quality of their portfolio has not deteriorated as much as price movement would suggest.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
F&C	(1.7)	(1.3)	2.2	n/a	1.7
3 Month LIBOR + 3%	0.9	3.6	3.5	n/a	3.6
Relative Performance	(2.5)	(4.8)	(1.3)	n/a	(1.9)

* 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:

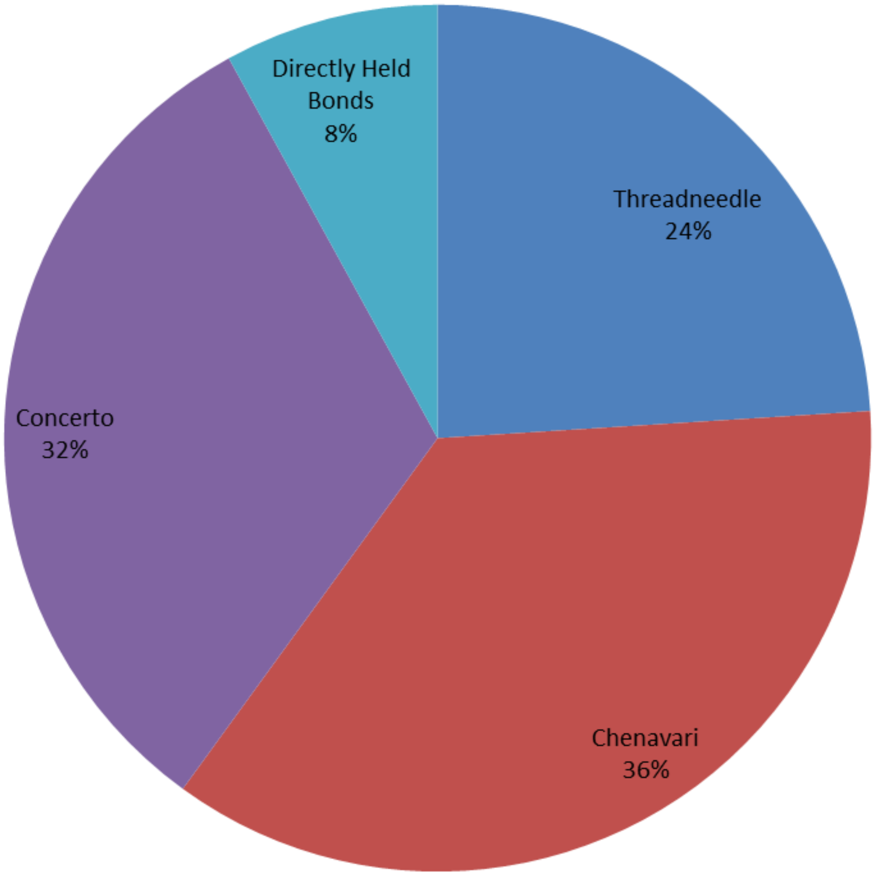
Threadneedle	Interest rates, currency
Chenavari	Credit
Concerto	Credit

Hymans Robertson View

Ben Fox continues to manage the Fund, and is supported by a significant team of macro, quant and multi strategy specialists. The Fund will be re-branded as "F&C

Absolute Return Bonds" at the end of February, when the return target on the Fund will also be increased to LIBOR+3% (from the current LIBOR+2.5% target) . The full transfer process and regulatory approval may take up to 20 weeks, however the fund can be marketed as F&C earlier than this with the caveat "awaiting regulatory approval". The Fund size currently stands at c.£115m, and the re-branding exercise allows F&C to actively market the Fund to potential new investors. Fox believes that there are sufficient attractive investment opportunities to merit the increased target.

The pie chart below shows the allocation as at 31st December 2014



Lincolnshire Pension Fund
Alternative Investments – Morgan Stanley
Quarterly Report December 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 30.09.14	Value at 31.12.14
£154,652,811	£155,911,580

Performance

Morgan Stanley produced a negative return of 1.13% during the quarter and underperformed their target by 2.2%. Commodities, frontier equity and expanded credit strategies detracted given the sharp decline in oil prices, the continued strength of the USD and widening of spreads. However, positive manager selection within all of these asset classes partially mitigated their negative returns. Furthermore, manager selection was the largest driver of returns, while strategic allocation detracted. Tactical decisions were muted for the quarter. Within manger selections, infrastructure, frontier equity and hedge funds drove outperformance, whereas global macro and inflation linked assets underperformed.

	Quarter %	1 Year %	3 Year* %	5 Year* %	Inception* %
Morgan Stanley	(1.1)	1.9	6.1	n/a	5.2
3 Month LIBOR + 4%	1.2	4.7	4.7	n/a	4.8
Relative Performance	(2.2)	(2.6)	1.3	n/a	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;

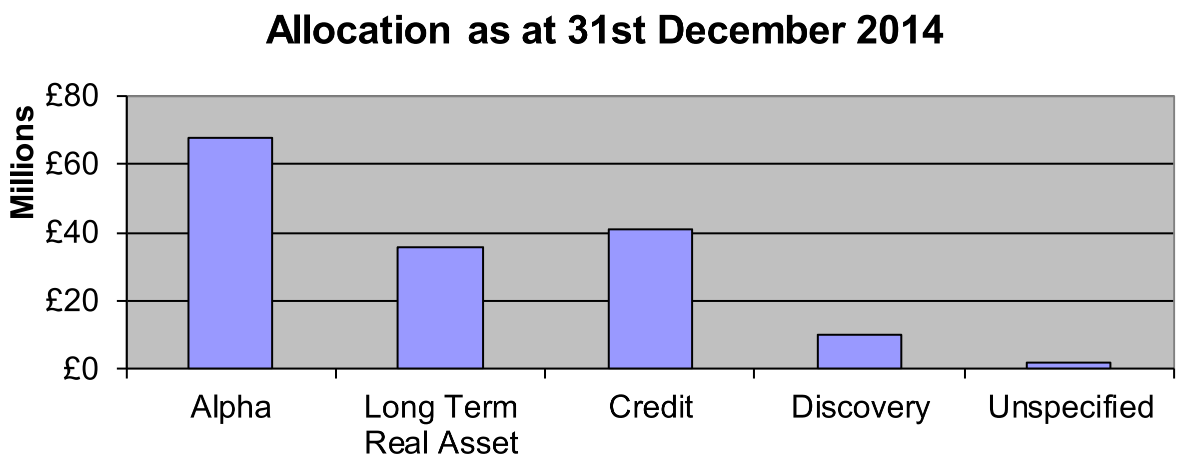
Alpha – These are pure return seeking products based on Manager skill. The Alpha investments include Hedge Funds, Global Tactical Asset Allocation (GTAA) and Active Currency.

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.

Unspecified – These are cash balances held with Morgan Stanley.



Portfolio Positioning

During the quarter Morgan Stanley maintained a relatively low weight to commodities given oversupply dynamics, but modestly increased their exposure as the recent sell-off provides an attractive entry point. They maintain a relatively low weight to real estate securities given the potential for rising interest rates in the US to negatively affect the relative attractiveness of property yields. They made an allocation mid-year to listed infrastructure and recently increased their REIT's exposure, where they believe their dividend paying characteristic will be valued by investors seeking safety and as a potential buffer to equity market pullbacks.

Hymans Robertson View

Hymans continue to rate Morgan Stanley a "5-preferred manager" for Diversified Alternatives. The team responsible for this portfolio remains highly stable and the three portfolio managers, Joe McDonnell in London, Ryan Meredith and Rui de Figueiredo in New York remain dedicated to managing this mandate. There have been no joiners or leavers from the team over the fourth quarter. Hedge Funds have always been a core strategic allocation within the portfolio due to what Morgan Stanley believes to be their attractive characteristics. However, the group has recently launched a liquid alternatives strategy which seeks to replicate some of the returns of hedge fund strategies but in a more liquid and transparent approach, and also with lower fees. Going forward Morgan Stanley may re-balance some of the hedge fund investments into this strategy. The Alternative Investment partners business continues to grow with assets under management of £24bn, of which just over £3bn is in diversified alternatives mandates. There have been no other significant developments over the quarter to end 31st December 2014.

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 3.16% which is slightly ahead of the benchmark. Managers have had mixed returns with seven 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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