

## Regulatory and Other Committee

**Open Report on behalf of Andrew Crookham,  
Executive Director - Resources**

Report to:	<b>Pensions Committee</b>
Date:	<b>15 October 2020</b>
Subject:	<b>Performance Measurement Annual Report</b>

**Summary:**

This report sets out the Pension Fund's longer term investment performance for the period ending 31<sup>st</sup> March 2020.

**Recommendation(s):**

That the Committee note the report.

## Background

### 1 INTRODUCTION

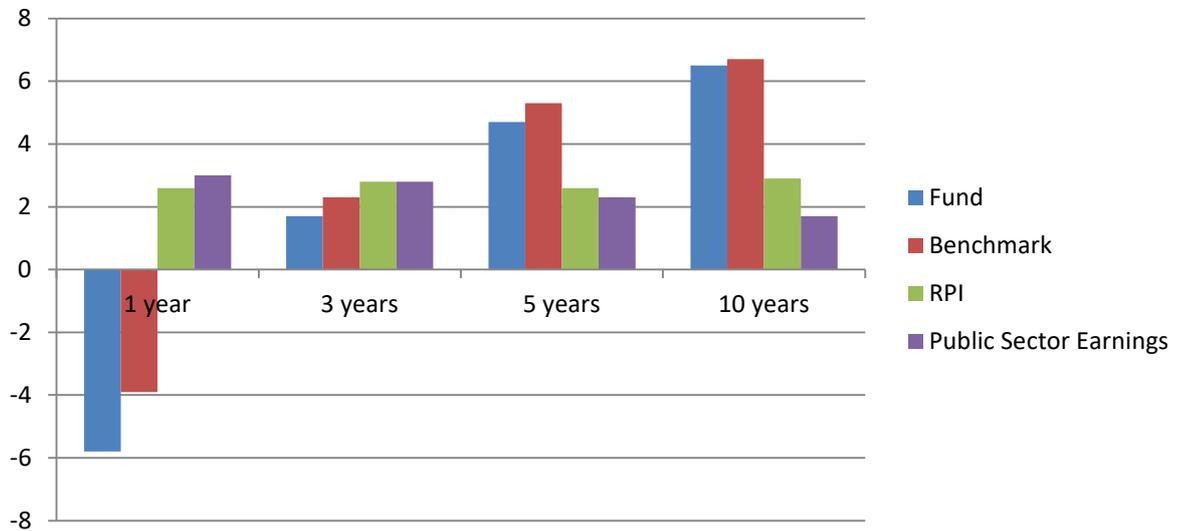
- 1.1 The Pension Fund uses two suppliers for the measurement of the Fund's performance. Northern Trust, the Fund's custodian (since 1 April 2019), calculates the Fund's investment performance and compares it with the returns of the strategic asset allocation benchmark (i.e. the return achieved by the mix of assets as recommended by the Actuary) and PIRC 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 0.75% per annum.

### 2 LONGER TERM PERFORMANCE FOR YEAR ENDED 31 MARCH 2020

- 2.1 The short term performance of the Fund and the performance of its managers are reported in the quarterly Investment Management report. This report focuses 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 2019, the Actuary has calculated the employers contribution strategy based on an assumed annual return of 4.0% over the long term.

2.2 The graph and table below shows 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 31/3/2020**



	1 year %	3 years annualised %	5 years annualised %	10 years annualised %
Retail Prices Index increases	2.6	2.8	2.6	2.9
Public sector average Earnings increases	3.0	2.8	2.3	1.7
<b>LCC Fund performance</b>	<b>(5.8)</b>	<b>1.7</b>	<b>4.7</b>	<b>6.5</b>
<b>LCC Benchmark Performance</b>	<b>(3.9)</b>	<b>2.3</b>	<b>5.3</b>	<b>6.7</b>
<b>Relative Performance</b>	<b>(2.0)</b>	<b>(0.6)</b>	<b>(0.6)</b>	<b>(0.2)</b>

**2.3 10 Year Returns**

The Fund's performance over ten years, at 6.5%, is slightly behind the Fund's benchmark return of 6.7%. This return is well ahead of both inflation and average earnings over the last ten years, to which the scheme's liabilities are linked, which were 2.9% and 1.7% p.a. respectively. The biggest impact, either negative or positive in each year, generally comes from the stock selection of the managers, rather than the Fund's position against its strategic benchmark.

## 2.4 5 Year Returns

Five year returns of 4.7% per annum are ahead of both price and pay inflation. The Fund's actual performance is behind the strategic benchmark return of 5.3%. This reflects the underperforming managers in 2016 and 2020.

## 2.5 3 Year Returns

Three year returns, at 1.7%, are behind of both inflation and average earnings, and also ahead of the strategic benchmark return of 2.3%. This reflects the underperformance of the Global ex UK manager.

## 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 each of the last ten years compared to the Benchmark is set out in the table below. There is an equal split between stock selection and asset allocation in terms of detractors across the ten year period.

3.5 The poor performance of Invesco in the year ended March 2020 was the key contributor to the overall Fund's underperformance.

3.6 Under asset pooling, the Pensions Committee will remain responsible for the asset allocation, however Border to Coast will be accountable for the stock selection element of the Fund's performance, as for any appointed external manager.

### Long Term Performance Analysis

Year ended March	Fund %	Benchmark %	Relative Performance %	Attributed to Asset allocation %	Attributed to Stock Selection %
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	0.1	1.1

<b>2014</b>	6.3	6.2	<b>0.1</b>	0.2	(0.1)
<b>2015</b>	12.3	12.4	<b>(0.1)</b>	(0.1)	0.0
<b>2016</b>	0.0	1.4	<b>(1.4)</b>	(0.6)	(0.8)
<b>2017</b>	19.8	19.3	<b>0.3</b>	0.0	0.3
<b>2018</b>	3.3	3.0	<b>0.3</b>	(0.4)	0.7
<b>2019</b>	8.2	8.1	<b>0.1</b>	0.0	0.1
<b>2020</b>	(5.8)	(3.9)	<b>(2.0)</b>	(0.3)	(1.6)

#### **4 PIRC LOCAL AUTHORITY UNIVERSE**

- 4.1 The PIRC Local Authority (LA) Universe is an aggregation of 63 funds covering £180bn of assets within the LGPS sector, and is used for peer group comparisons. This represents some two thirds of local authority pension fund assets and includes all of the Welsh and Northern Pools, all bar one of the London Pool, and with funds from all other pools except Central.
- 4.2 Investment market volatility is nothing new. Many will have lived through the irrational exuberance of the Dot-Com bubble, the market crash now termed the Global Financial Crisis, the Asian, Chinese and Russian market crises, the Japanese equity bubble, the list goes on. However unlike previous market crashes no one could have predicted the events that brought the world to a virtual standstill at the start of 2020. The first quarter of 2020 saw global equity markets lose a quarter of their value while credit markets also fell, property funds were closed as managers struggled to value assets in these new times. But the results for the year were not as bad as might have been expected from the gloomy position we found ourselves in at the end of March. Equities had fallen, but from historic highs, and funds, now more diversified than ever, saw their total assets fall, but only by an average of 4.8%.
- 4.3 Asset class returns differed significantly. Private equity was the best performing asset class at 12.1%, followed by UK Government bonds at 8.1%. Equities were the worst performing asset class, down 12.5% overall, and within that UK equities fell the most returning -18.2%.
- 4.4 Since the 1990's, Funds have been using specific strategic benchmarks linked to their individual liability profiles, rather than a standard asset allocation. This means that comparison across the Universe can be misleading, as funds are trying to meet their own return requirements rather than compete for the highest return.
- 4.4 Given this move to fund specific strategic benchmarks, the peer group comparison is only a reference point, and not directly comparable. Strategic benchmarks, and the overall return requirement, is linked to the individual liability profiles of each fund, and their funding levels. The most important performance comparison is actual performance against the individual funds strategic benchmark.

- 4.5 The table below shows how the strategic asset allocation for the Lincolnshire Fund (currently in transition) compares with the average Local Authority Pension Fund in 2020 and 2019.

Asset Class	Lincolnshire	LA Average	
		2020	2019
Equities	55.0	51	55
Bonds	12.5	21	19
Property	10.5	9	9
Alternatives	21.0	13	8
Diversified Growth	0.0	3	3
Cash	1.0	3	3

- 4.6 Across the LA Universe, there has been a continuing movement to reduce equities and increase bonds and alternative assets.
- 4.7 The Fund structure is higher in equities and lower in bonds, which had an impact of reducing relative performance by roughly 0.5%.
- 4.8 The performance of the Fund against the average of those Funds subscribing to the Local Authority universe ranked at the 70<sup>th</sup> percentile, having been at the 10<sup>th</sup> percentile last year.
- 4.9 The table below shows the position of the Lincolnshire Fund over 1, 3, 5 and 10 years, alongside the top and bottom returns across the universe.

	1 year %	3 years annualised %	5 years annualised %	10 years annualised %
<b>LCC Fund performance</b>	<b>(5.8)</b>	<b>1.7</b>	<b>4.7</b>	<b>6.5</b>
<b>Universe Average</b>	<b>(4.8)</b>	<b>1.9</b>	<b>5.2</b>	<b>6.9</b>
<b>Ranking</b>	<b>70</b>	<b>48</b>	<b>54</b>	<b>76</b>
<b>1st percentile</b>	<b>1.8</b>	<b>5.9</b>	<b>8.1</b>	<b>9.4</b>
<b>100th percentile</b>	<b>(11.2)</b>	<b>(0.8)</b>	<b>2.9</b>	<b>5.2</b>

## 5 Conclusion

- 5.1 The Pension Fund's investment performance of 6.5% over the 10 year period ended 31<sup>st</sup> March 2020 was slightly behind the strategic benchmark of 6.9%. The Fund is seeking to outperform the Benchmark by 0.75% per annum over rolling three year periods. Annualised returns over five and ten year periods are ahead of inflation in pay and prices. At an absolute level, the ten year performance is ahead of the current actuarial assumption for return of around 4.0% per annum.

5.2 Looking at the last year, there were negative contributions from both stock selection and asset allocation in the year ended March 2020, and the Fund was ranked at the 70<sup>th</sup> percentile of the Local Authority Universe.

## **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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