PENSIONS PANEL

14 December 2016

Title: Pension Fund Quarterly Monitoring 2015/16 – July to September 2016	
Report of the Strategic Director, Finance & Investment	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
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Accountable Director: Kathy Freeman, Finance Director	
Accountable Strategic Director: Jonathan Bunt, Strategic Director – Finance and Investment	

Recommendations

The Panel is recommended to note:

(i) the progress on the strategy development within the Pension Fund;

(ii) the currency hedges that were placed on the Fund's passive equity mandate on the 30th of September and 7th of October 2016;

(iii) the daily value movements of the Fund's assets and liabilities outlined in Appendix 1; and

(iv) the quarterly performance of pension funds collectively and the performance of the fund managers individually;

1. Introduction and Background

1.1 This report provides information for employers, members of London Borough of Barking and Dagenham Pension Fund ("the Fund") and other interested parties on how the Fund has performed during the quarter 1 July 2016 to 30 September 2016 ("Q3"). The report updates the Panel on the Fund's investment strategy and its investment performance. Due to the technical nature of this report, Appendix 2 provides a definition of terms used in this report and Appendix 3 sets out roles and responsibilities of the parties referred to throughout this report.

1.2 A verbal update on the unaudited performance of the Fund for the period 1 October to 12 December 2016 will be provided to Members at the Pension Panel.

2. Third Quarter Market Performance

The latest quarter opened with the British vote to leave the European Union still reverberating through markets. The initial shock passed quickly enough and equity markets rebounded; within three weeks, the US stock market was at a record high and while European markets took longer to regain pre-Brexit levels, most achieved strong returns in the quarter. Accommodative central banks bolstered equity investors; the Bank of England (BOE) followed through on its commitment to cut interest rates to cushion the impact of Brexit, while the European Central Bank (ECB) and US Federal Reserve (Fed) kept interest rates unchanged.

The IMF reacted to the Brexit vote by trimming its global growth forecast, along with a more sizeable downgrade of UK prospects, but the macro-economic backdrop has since proven resilient. Data releases indicate the UK economy has held up better than expected, although how much is due to a weak pound and lower interest rates remains to be seen. The British pound stabilised over the quarter, although it still lost ground against the major currencies as the BOE cut its key lending rate to 0.25% from 0.50% in August and signalled a further cut if necessary. Over the quarter Sterling lost 4% against the Euro and the Yen and 3% against the US Dollar.

Across asset markets, there was a bias for riskier assets. From a UK investor perspective, Emerging market and Pacific ex Japan equity markets were the best performers, returning more than 12% over the quarter. Europe returned 9%, North America 7% and the FTSE All Share returned just short of 8% - mining, technology and bank stocks outperformed, while telecoms and utilities lagged the market.

Fixed income markets began the quarter with yields close to record lows, falling further for a time as a US rate hike seemed unlikely and as the Bank of England cut its benchmark rate to 0.25%. In the absence of particularly negative post-Brexit economic data, the investor dash for fixed income assets began to unwind. There was some reversal of bond market gains as Q3 progressed, although many still posted positive returns. The BAML Broad market index returned nearly 4% and the FTSE Index Linked >5 year index returned 11%.

Property returned -2% over the quarter, the first negative quarterly return since Q2 2009. Three-month GBP LIBOR fell from 0.56% to 0.38% as the Bank of England cut interest rates.

3. Overall Fund Performance

3.1 The Fund's externally managed assets closed Q3 valued at £844.2m, an increase of £53.4m from its value of £790.8m as at 30 June 2016. The cash value held by the Council as at 31 March 2016 was £19.6m giving a total Fund value of £863.8m.

3.2 For Q3 the Fund returned 5.3%, net of manager and custodian fees, outperforming its benchmark return of 4.4% by 0.9%. Over one year the Fund returned 17.4%, outperforming its benchmark of 16.6% by 0.8%. Over three years the Fund trails its benchmark by 0.7%, providing a return of 9.4, which exceeds the actuarial return target for the fund of 4.7%.

3.3 The Fund's 2014, 2015 and Q3 2016 quarterly returns, its 1, 2, 3 and year returns are provided in table 1 below:

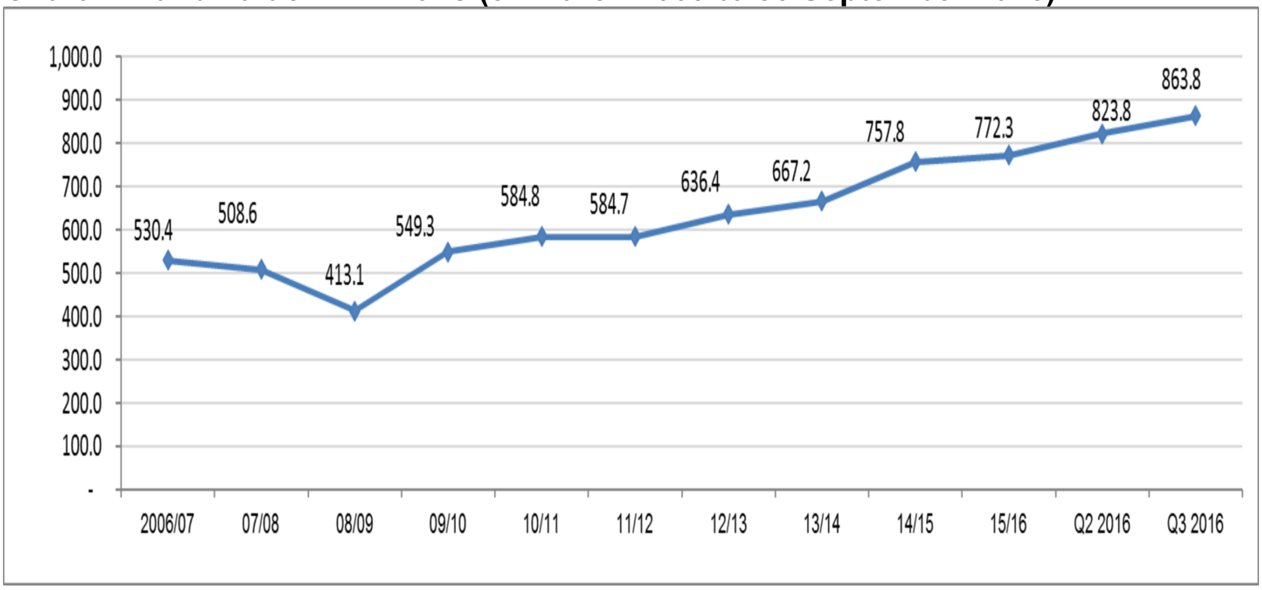
Table 1: Fund's Q3 2016, 2015 and 2014 Quarterly Returns and yearly returns

Year	2016			2015				2014	1	2	3	5
Period	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4	yr	yrs	yrs	yrs
Actual Return	5.3	4.2	2.5	4.4	(2.5)	(3.3)	10.0	3.6	17.4	12.1	9.4	10.0
Benchmark	4.4	4.7	2.0	4.5	(1.4)	(1.8)	10.7	3.3	16.6	13.2	10.1	10.7
Difference	0.9	(0.5)	0.5	(0.1)	(1.1)	(1.5)	(0.7)	0.3	0.8	(1.1)	(0.7)	(0.7)
WM Position*	N/A	N/A	18th	41st	23rd	74th	N/A	34th	N/A	N/A	N/A	N/A

* Figures for the LGPS comparisons, provided by State Street, which have previously been provided are no longer available from 1 July 2016 due to State Street exiting the market.

3.4 Appendix 1 illustrates changes in the market value, the liability value, the Fund's deficit and the funding level from 31 March 2013 to 25 November 2016. Members are asked to note the significant changes in value and the movements in the Fund's funding level. Chart 1 below shows the Fund's value since 1 July 2007.

Chart 1: Fund value in millions (31 March 2009 to 30 September 2016)



3.5 Stock selection contributed 0.7% of the overall, with asset allocation contributed 0.2% for the quarter. Table 2 shows the change in market value during the quarter by each fund manager, including transactions and profits/ (losses).

Table 2: Fund manager market value and asset allocation at 30 September 2016

Fund Manager	Mandate	Value at 31/03/2016	Trans-actions	Gain / loss	Value at 30/06/2016
		£000s	£000s	£000s	£000s
Aberdeen	Diversified Alternative	52,020	55	421	52,496
Baillie Gifford	Global Equities	131,386		15,860	147,246
BlackRock	Property	40,089	235	(1,635)	38,689
Hermes GPE	Infrastructure	59,881	3,840	991	64,712
Kempen	Global Equities	119,731	90	12,165	131,986
M&G	Senior Loans	5,787	(249)	60	5,598
Newton	Absolute Return	57,129		852	57,981
Pyrford	Absolute Return	78,083		2,414	80,497
Schroders	Property	16,812	5,151	487	22,450
Standish	Global Credit	62,719	66	871	63,656
UBS Bonds	Passive Bonds	35,681		824	36,505
UBS Equities	Passive Equities	131,443		10,769	142,212
London CIV	Equity Investment	150		0	150
	Cash	32,238		(12,652)	19,586
Total Fund		823,149	9,188	31,428	863,765

3.6 The fund manager's performance has been scored using a quantitative analysis compared to the benchmark returns, defined below. Based on these criteria the fund manager Q3 performances are shown in table 3.

	RED- Fund underperformed by more than 75% below the benchmark
Δ	**A**MBER- Fund underperformed by less than 75% below the benchmark.
O	**G**REEN- Fund is achieving the benchmark return or better

3.7 Table 3 highlights the best performers during Q3 were unhedged equity, bonds and diversified growth. Schroders provided a good return following the previous quarters underperformance. Blackrock and Aberdeen underperformed their benchmark and meetings have been arranged with both managers to discuss the underperformance.

Table 3 – Fund manager Q3 performance

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Aberdeen	0.3	1.1	(0.8)	Δ
Baillie Gifford	12.1	8.5	3.6	O
BlackRock	(3.5)	(0.7)	(2.8)	Δ
Hermes GPE	1.6	1.4	0.2	O
Kempen	10.2	7.9	2.3	O
M&G	1.1	1.1	0.0	O
Newton	1.5	1.1	0.4	O
Pyrford	3.1	1.9	1.2	O
Schroders	3.8	0.1	3.7	O
Standish	1.4	1.1	0.3	O
UBS Bonds	2.3	2.3	0.0	O
UBS Equities	8.2	8.2	0.0	O

3.8 Over one year, (table 4 below), equities, bonds, diversified growth and infrastructure provided double digit returns. Standish significantly underperformed its benchmark but has met its target over the two quarters since they presented at the June Panel.

Table 4 – Fund manager performance over 12 months

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Aberdeen	3.3	4.4	(1.1)	Δ
Baillie Gifford	29.7	28.3	1.4	O
BlackRock	1.5	3.5	(2.0)	Δ
Hermes GPE	10.3	5.6	4.7	O
Kempen	29.4	28.2	1.2	O
M&G	4.4	4.4	0.0	O
Newton	11.3	4.4	6.9	O
Pyrford	10.9	6.9	4.0	O
Schroders	1.7	3.3	(1.6)	Δ
Standish	(1.0)	5.2	(6.2)	
UBS Bonds	12.3	12.3	0.0	O
UBS Equities	27.9	27.9	0.0	O

3.9 Over two years, (table 5 below), all mandates are positive, with returns ranging from 0.6% with Standish to 17.3% with Baillie Gifford. Standish has significantly underperformed its benchmark by 5% over the two-year period.

Table 5 – Fund manager performance over two years

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Aberdeen	3.4	4.4	(1.0)	Δ
Baillie Gifford	17.3	14.7	2.6	O
BlackRock	6.1	8.5	(2.4)	Δ
Hermes GPE	9.3	5.6	3.7	O
Kempen	13.9	15.3	(1.5)	Δ
M&G	4.5	4.4	0.1	O
Newton	6.3	4.4	1.9	O
Pyrford	6.4	6.3	0.1	O
Schroders	7.0	8.4	(1.4)	Δ
Standish	0.6	5.6	(5.0)	
UBS Bonds	10.3	10.3	0.0	O
UBS Equities	15.3	15.0	0.3	O

4. Asset Allocations and Benchmark

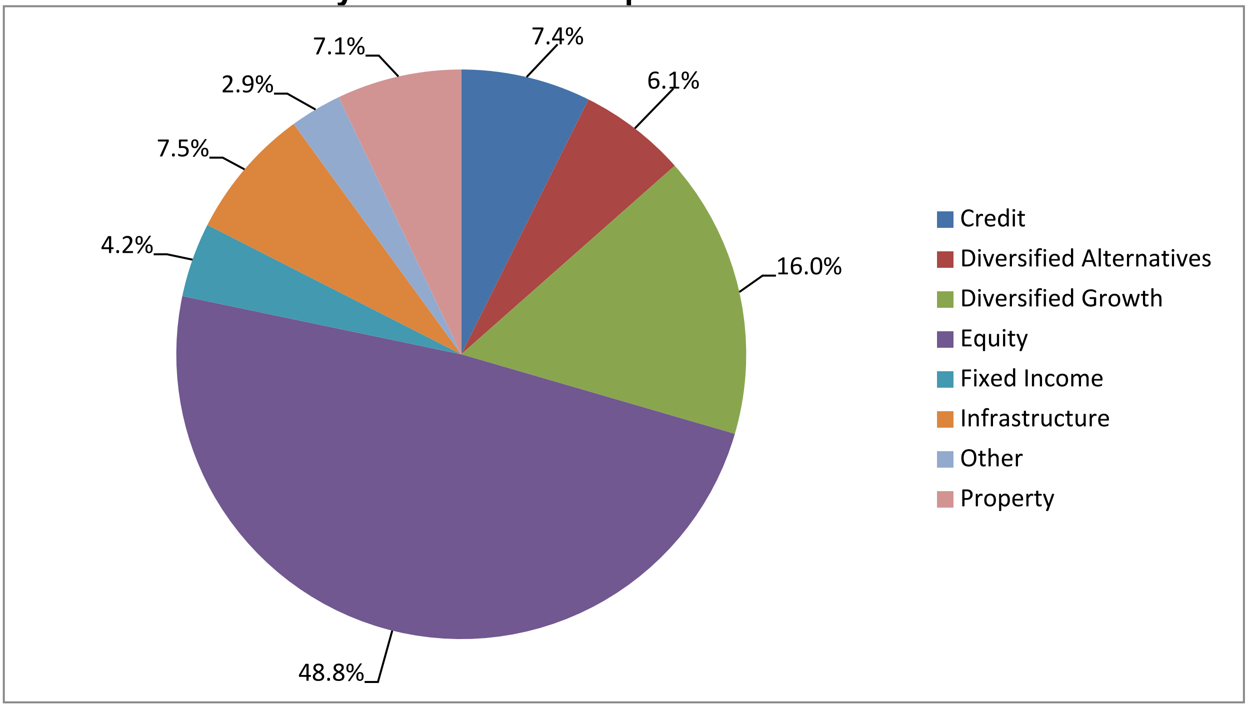
4.1 Table 6 outlines the Fund's strategic asset allocation, asset value and benchmarks:

Table 6: Fund Asset Allocation and Benchmarks as at 30 September 2016

Fund Manager	Asset (%)	Market Values (£000)	Benchmark
Aberdeen	6.1%	52,496	Libor + 4% (net of fees)
Baillie Gifford	17.0%	147,246	MSCI AC World Index
BlackRock	4.5%	38,689	IPD PPF All Balanced Property Funds
Hermes GPE	7.5%	64,712	Target 5.9% per annum
Kempen	15.3%	131,986	FTSE All World Developed
M&G	0.6%	5,598	None
Newton	6.7%	57,981	Libor + 4% (net of fees)
Pyrford	9.3%	80,497	One month LIBOR plus 4%
Schroders	2.6%	22,450	RPI plus 5%
Standish	7.4%	63,656	IPD PPF All Balanced Property Funds
UBS Bonds	4.2%	36,505	6% Target Return
UBS Equities	16.5%	142,212	FTSE All Stock Gilt Index
London CIV	0.0%	150	MSCI World NDR Index
Cash	2.3%	19,586	One month LIBOR
Total Fund	100.0%	863,765	

4.2 The percentage split between managers is graphically shown in the pie chart below.

Chart 2: Fund Asset by Asset as at 30 September 2016



5. Fund Manager Performance

5.1 Kempen

	2016			2015				2014	One	Two	Since Start
Kempen	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**6/2/2013**
£131,986	**%**	%	%	%	%	%	%	%	%	%	%
Actual Return	**10.2**	5.8	5.9	7.5	(5.8)	(5.7)	7.7	2.1	29.4	13.9	9.4
Benchmark	**7.9**	9.7	2.2	8.4	(4.8)	(5.3)	7.5	5.0	28.2	15.3	13.1
Difference	**2.3**	(3.9)	3.7	(0.9)	(1.0)	(0.4)	0.2	(2.9)	1.2	(1.5)	(3.7)

Reason for appointment

Kempen were appointed as one of the Fund's global equity managers, specialising in investing in less risky, high dividend paying companies which will provide the Fund with significant income. Kempen holds approximately 100 stocks of roughly equal weighting, with the portfolio rebalanced on a quarterly basis. During market rallies Kempen are likely to lag the benchmark.

Performance Review

During the quarter Kempen completed their quarterly rebalance, buying and selling nine companies. Purchases included:

- Wells Fargo - franchise is intact despite its current reputational headwinds.
- Severstal (Russian steel operator) - low production costs and limited net debt.
- SKF (industrial ball bearings) - new CEO, undergoing a transformation;
- BT Group as the share price offered a compelling entry point
- Abbvie, Exelon Corp, JSR Corp, Life Storage and AMEC Foster Wheeler.

Most of the disposals were driven by stocks crossing their 3% threshold, due to strong share price performance, including Procter & Gamble, Cullen/Frost Bankers, Merck, Copa Holdings; and Hancock Holdings. Telenor, Royal Mail, Boardwalk Real Estate and LaSalle Hotel Properties were sold as the investment case no longer offered a good risk adjusted return.

Outlook

Kempen have seen high volatility among their holdings despite there being limited changes the firms intrinsic value. Kempen believe that their rebalancing process continues to add value by taking advantage of this volatility. Overall market multiples remain elevated, but the dispersion both within and between sectors has increased.

Kempen focus is on finding companies with sustainable dividends that can be bought at a discount to their estimate of intrinsic value. Kempen base their estimate on the Earnings Power Value (EPV) framework of the Columbia Business School. EPV allows us to separate the three valuation components: asset value, earnings power and growth value. This framework improves their ability to analyse what Kempen are paying for, and gives insight into whether a stock is priced with a margin of safety.
The Fund now has a forward yield of around 4.9%.

5.2 Baillie Gifford

	2016			2015				2014	One	Two	Since Start
Baillie Gifford	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**6/2/2013**
£147,246	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**12.1**	6.9	0.3	10.4	(5.8)	(4.9)	9.1	6.5	29.7	17.3	15.6
Benchmark	**8.5**	8.8	2.9	8.1	(5.9)	(5.1)	7.6	4.5	28.3	14.7	13.0
Difference	**3.6**	(1.9)	(2.6)	2.3	0.1	0.2	1.5	2.0	1.4	2.6	2.6

<u>Reason for appointment</u>

Baillie Gifford (BG) is primarily a bottom-up, active investor, seeking to invest in companies that it believes will enjoy sustainable competitive advantages in their industries and which will grow earnings faster than the market average. The aim of the Global Alpha investment process is to produce above average long term performance by picking the best growth stocks available around the world by combining the specialised knowledge of BG's investment teams with the experience of their most senior investors. BG holds approximately 90-105 stocks.

The manager was appointed as it is a long-term stock picker but with a high emerging market weighting. The lower number of stocks held compared to the Fund's previous equity managers is also seen as an advantage. The active share of the portfolio remains very low. The Fund holds its investment with BG through the London CIV, following the transfer of its assets on the 11th July 2016.

<u>Performance Review</u>

Prior to the unexpected triumph of the Leave campaigners BG considered which companies in the mandate would be most affected by the Referendum. BG identified five UK-listed holdings (Prudential, Wolseley, Rolls Royce, Hays and Aggreko) which might suffer from post referendum uncertainty. However, these companies generate most their profits and revenues overseas.

Of the European holdings in the portfolio, BG felt the most affected would be Irish companies, Ryanair, Bank of Ireland and CRH along with two other stocks with material UK and other Western European exposure in Carlsberg and Svenska Handelsbanken. This analysis was broadly correct in that the stocks mentioned above include most of the companies whose share prices were the hardest hit immediately following the referendum result.

Performance during the quarter was behind the index. Whilst this is disappointing, BG hold the view that they cannot accurately anticipate the outcome of a closely fought referendums, or hedge against its outcome but focus on the fundamentals and, in the short run, politics can swamp these.

BG remains confident in the portfolio's positioning, which continues to be well-diversified across a range of growth companies, and are pleased with the operational performance. BG holds a view that the market weakness has created some exciting opportunities to invest in high quality companies at attractive valuations.

5.3 UBS Equities

	2016			2015				2014	One	Two	Since Start
UBS Equities	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**31/8/2012**
£142,212	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**8.2**	8.7	2.4	8.6	(4.8)	(5.2)	7.7	4.9	27.9	15.3	15.8
Benchmark	**8.2**	8.7	2.4	8.6	(5.0)	(5.3)	7.6	4.8	27.9	15.0	15.8
Difference	**0.0**	0.0	0.0	0.0	0.2	0.1	0.1	0.1	0.0	0.3	0.0

Reason for appointment

UBS were appointed as the Fund’s passive equity manager to reduce the risk from underperforming equity managers and provides a cost-effective way of accessing the full range of developed market equity growth. UBS track the developed world market benchmark and there will only be an issue with performance were the manager to vary significantly from the benchmark, either positively or negatively.

Performance

Global equities had risen earlier in the quarter, as economic data in the US and Eurozone improved from the weaker data seen in the first three months of the year. Central bank activity remained in focus, with an increased likelihood of further rises in interest rates in the US. The oil price continued to rally sharply from February's lows, and investors' concerns over the pace of growth in China eased.

Post the EU referendum in the UK, it was noticeable that after initial sharp losses, equities enjoyed one of their best weeks of the year. US equity markets benefited from a resetting of interest rate expectations back to a 'lower for longer' outlook.

Japanese equities had a difficult quarter on a relative basis, as the failure of the Bank of Japan to meet expectations for further policy initiatives in the wake of weak economic data saw the Japanese yen strengthen sharply. European equities fared poorly later in the quarter due to increased political uncertainties.

UBS Bonds

	2016			2015				2014	One	Two	Since Start
UBS Bonds	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**20/8/2013**
£36,505	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**2.3**	6.2	5.0	(1.2)	3.1	(3.4)	2.2	6.3	12.3	10.3	8.4
Benchmark	**2.3**	6.2	5.0	(1.2)	3.1	(3.4)	2.2	6.3	12.3	10.3	8.4
Difference	**0.0**	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Reason for appointment

UBS were appointed as the Fund’s passive bond manager to allow the Fund to hold a small allocation (5%) of UK fixed income government bonds.

Performance

Government bond yields fell to record lows reflecting their safe-haven status amidst market turmoil post the referendum result and expectations for lower growth globally.

5.4 BlackRock

	2016			2015				2014	One	Two	Since Start
BlackRock	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**30/11/2012**
£38,689	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**(3.5)**	**1.3**	**1.2**	**2.5**	**2.5**	**2.9**	**2.2**	**3.1**	**1.5**	**6.1**	**9.2**
Benchmark	**(0.7)**	0.1	1.1	3.0	3.0	3.1	2.8	4.6	3.5	8.5	11.4
Difference	**(2.8)**	1.2	0.1	(0.5)	(0.5)	(0.2)	(0.6)	(1.5)	(2.0)	(2.4)	(2.2)

Reason for appointment

In March 2012, a large portion of the Fund's holdings with Rreef were transferred to BlackRock (BR). The transfer to BR provides the Fund with access to a greater, more diversified range of property holdings within the UK.

Transactions

The Fund transacted four sales for a total of £140m, the most significant of which was a strategic move to down weight its exposure to Central London Office. A substantial portfolio sale of 11 smaller, secondary assets was exchanged after the quarter end, which had the effect of cleaning up most the remaining non-core holdings in the Fund.

Referendum Result Impact on UK Property

Given the volatility after the Brexit vote was caused by a political crisis rather than a financial one, the Conservative party's ability to fill its leadership void swiftly, had a significant stabilising effect.

Reactions to political events continue to dominate as the UK government and the EU determine what Brexit looks like. This creates periods of volatility and the need for a defensive approach is a preferable position. There is a significant amount of capital moving around the global financial markets seeking investments looking for yield. This is magnified in the UK by lower for even longer interest rates and a fall in Sterling.

UK real estate offers a relatively high yield, a balanced supply and demand dynamic, benefits from expansionary monetary policy and is less fully valued than other asset classes. It therefore looks set to continue to attract domestic and international capital.

Valuations

Although values reduced post the referendum vote, the depth of capital returning to the market helped put a floor under pricing declines, which ended up surprising on the upside. For much of Q3 valuers maintained a caveat expressing a greater risk around the accuracy of valuations due to the market uncertainty following the referendum and a lack of transactional evidence. As the quarter progressed these caveats were watered down and eventually removed, as valuations were adjusted, and what turned out to be a relatively liquid market started to provide post referendum evidence.

BlackRock experienced a 2.5% reduction in values over Q3, with a broad dispersion between Student Housing, Primary Healthcare and Industrials, which experienced little or no decline, and Central London Offices which averaged a 7.5% reduction.

5.5 Schroders Indirect Real Estate

	2016			2015				2014	One	Two	Since Start
Schroder	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**06/08/2010**
£22,450	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**3.7**	(5.2)	0.8	2.4	3.0	2.6	2.8	3.9	1.7	7.0	6.3
Benchmark	**(0.7)**	0.1	1.1	2.8	3.0	3.1	2.8	4.6	3.3	8.4	8.1
Difference	**4.4**	(5.3)	(0.3)	(0.4)	0.0	(0.5)	0.0	(0.7)	(1.6)	(1.4)	(1.8)

Reason for appointment

Schroders is a Fund of Fund manager appointed to manage a part of the Fund's property holdings. The mandate provides the Fund with exposure to 210 underlying funds, with a total exposure to 1,500 highly diversified UK commercial properties.

Market summary

While early indications are that the UK economy has fared better in the quarter following the EU referendum than predicted, market uncertainty has unsurprisingly led to value declines in UK commercial real estate. However, occupier demand has remained firm since June 2016, reflecting low vacancy rates and a limited level of new building in recent years. During the quarter, increased political stability, a cut in interest rates and signs of continued economic growth calmed investor sentiment. This has been reflected in increased liquidity, smaller discounts in secondary market and a decrease in the fair value adjustments to fund pricing.

Strategy

Over recent quarters SIRE's strategy has been to increase the defensive qualities of the trust, favouring allocations such as core balanced funds, where returns are underpinned by income; and decreasing holdings where returns are driven by capital growth. In the third quarter, we selectively trimmed positions in funds where yields are low (West End of London Property Unit Trust) and where secondary market liquidity and pricing was relatively attractive (Threadneedle Property Unit Trust and UNITE UK Student Accommodation Fund).

Performance

Performance improved against benchmark over the quarter. Over 1 and 3 years, SIRE has underperformed its benchmark.

The top performing allocation over the quarter was the Ishares UK Property which returned 5.5% as real estate securities rebounded from their post-Brexit sell off. Although specialist funds such as the Industrial Property Investment Fund and The Leisure Fund Unit Trust outperformed, in aggregate value add holdings detracted.

Core balanced funds outperformed, led by Metro Property Unit Trust, Schroders' partnership vehicle investing in South East business space. The BlackRock UK Property Fund also outperformed, based on the mid-price valuation methodology used by the Trust, as the adjustment to its bid price was removed (bid -5%).

5.6 M&G / Prudential UK

	2016			2015				2014	One	Two	Since Start
M&G / Prudential	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**31/05/2010**
£5,598	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**1.1**	1.1	1.1	1.1	1.1	1.1	1.2	1.1	4.4	4.5	4.7
Benchmark	**1.1**	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.4	4.4	4.4
Difference	**0.0**	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.1	0.3

Reason for appointment

This investment seeks to maximise returns using a prudent investment management approach with a target return of Libor +4% (net of fees) and provides diversification from active bond management by holding the loans until their maturity. The strategy continues to meet its objectives and there were no issues in the quarter.

The portfolio maintained its seven senior loan investments with several medium sized institutions, with no changes to their respective credit ratings. The date of the last loan maturity is 2021, after which the investment will be wound up and the final distributions made.

5.7 Hermes

	2016			2015				2014	One	Two	Since Start
Hermes	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**19/11/2012**
£64,712	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**1.6**	2.5	5.9	0.3	1.7	1.1	1.3	4.1	10.3	9.3	11.0
Benchmark	**1.4**	1.4	1.4	1.4	1.4	1.4	1.4	1.4	5.6	5.6	6.0
Difference	**0.2**	1.1	4.5	(1.1)	0.3	(0.3)	(0.1)	2.7	4.7	3.7	5.0

Reason for appointment

Hermes were appointed as the Fund's infrastructure manager to diversify the Fund away from index linked fixed income, with the Fund's index linked government bonds used to fund Hermes. The investment duration is a five-year investment period and a base term of 18 years. At the March 2015 Panel, Members agreed to increase the Fund's allocation to Hermes to 10%, accessed via two limited liability partnerships. As the Fund already had an allocation of 5% to the Hermes Core partnership and a 2% allocation to the value-added partnership, the additional 3% was invested in the value-added partnership.

Holdings and performance

Hermes is invested directly in a variety of UK based infrastructure investments, including water companies, wind farms, solar energy, PFI and ports. The strategy also invests in value added investments include Eurostar, a secondary investment with Goldman Sachs and RREEF and an allocation to a water company. The strategy has performed well since initial funding with an average return of 11.0%. Each asset provides significant cash yields, which will provide a steady return both in terms of cash and capital appreciation.

5.8 Aberdeen Asset Management

	2016			2015				2014	One	Two	Since Start
Aberdeen	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**15/09/2014**
£52,496	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**0.3**	0.9	2.2	(0.1)	0.4	(0.6)	1.4	2.2	3.3	3.4	3.4
Benchmark	**1.1**	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.4	4.4	4.4
Difference	**(0.8)**	(0.2)	1.1	(1.2)	(0.7)	(1.7)	0.3	1.1	(1.1)	(1.0)	(1.0)

Reason for appointment

As part of the Fund's diversification away from equities Members agreed to tender for a Diversified Alternatives Mandate. Aberdeen Asset Management (AAM) were appointed to build and maintain a portfolio of Hedge Funds and Private Equity. All positions held within the portfolio are hedged back to Sterling.

Market Update and Performance Summary

The trading environment continues to be dominated by central bank policy actions. Speculation that the Bank of Japan (BOJ) would try engineer a steeper yield curve by reducing purchases of longer maturity bonds sparked a global sell-off in long term rates. There was a marked increase in the correlation between stocks and bonds during this period, with declines in bond prices occurring simultaneously with declines in high dividend sectors of the market such as real estate, utilities, and telecoms.

Financials benefited from the rise in long term rates and outperformed. The BOJ surprised markets in September by announcing an intention to use asset purchases to set the level of ten-year bond yields and global yield curves reversed much of the steepening that had occurred prior to the meeting. In addition, the Federal Reserve kept rates on hold in September, which also helped to stabilise demand.

In Europe and Japan, following a rally in July and August, equities faced headwinds from the strength of the euro and the yen, and both regions saw equities decline modestly in September. Emerging markets had stronger performance supported by both a rise in the price of oil and the dovish stance taken by the Federal Reserve. The holdings and a summary of the strategy and style is included in the table below:

Fund	Strategy / Style
Hedge Funds	
Field Street Fund	Fixed Income, Global Macro
Horizon Portfolio Ltd	Market Neutral
Kohinoor Series Three	Tail-risk protection
Obsidian Fund	Fixed Income Relative Value
Pharo Gaia Fund	Discretionary global macro, invests in emerging markets
Alteaus Overseas Fund	Discretionary global macro, focused on FX / commodities
Complus Asia Macro	Discretionary macro fund focused on Asia
Renaissance IDA	Statistical Arbitrage
BlackRock Fixed Income	Relative Value
Private Equity	
PAI Europe VI	Buyout Midcap
MML Capital Partners VI	Lower Mid Market

5.9 Pyrford

	2016			2015				2014	One	Two	Since Start
Pyrford	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**28/09/2012**
£80,497	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**3.1**	3.2	2.4	2.2	(0.5)	(2.5)	2.8	2.0	10.9	6.4	4.9
Benchmark	**1.9**	2.0	1.4	1.6	1.5	1.9	1.1	1.2	6.9	6.3	6.1
Difference	**1.2**	1.2	1.0	0.6	(2.0)	(4.4)	1.7	0.8	4.0	0.1	(1.2)

Reason for appointment

Pyrford were appointed as the Fund's absolute return manager (AR) to diversify from equities. The manager's benchmark is a fixed benchmark, which means that the manager is likely to outperform the benchmark significantly during market rallies.

AR managers can be compared to equities, which have a similar return target. When compared to equities, absolute return is likely to underperform when markets increase rapidly and to outperform equities during periods when markets suffer a sharp fall. 2013 and into 2014 could be classified as a significant market rally and therefore, in comparison to equities, Pyrford have underperformed.

Market Update and Performance Summary

At the end of July Pyrford reduced the equity exposure, after considering continued strength in equity markets, both domestic and global, by 5% to a model allocation of 30% equities, 67% bonds and 3% cash. The portfolio is now back to the same equity weighting as it was going into the financial crisis in 2008. This reflects the view that there is very little fundamental value in either equities or longer duration quality sovereign bonds and that capital market valuations do not discount the significant structural economic problems and material risks that exist.

The equity portfolio remains defensively invested in utilities, energy and telecommunications. Pyrford views these sectors as offering predictable revenue streams and attractive valuations. The focus of the portfolio is on balance sheet strength, profitability, earnings visibility and value.

No changes were made to the portfolio's currency hedging programme in the quarter, although Pyrford did sell US government bonds based on the team's view of the US dollar being significantly overvalued versus Sterling. In line with Pyrford's purchasing power parity analysis, only the Swiss franc exposure within the portfolio remains fully hedged, insulating the portfolio against any fall in the value of the currency.

High quality sovereign bond yields continued to fall in the quarter of the year. Pyrford retains a defensive stance by owning only short duration securities to protect the capital value of the portfolio from expected rises in yields. At the end of the quarter the modified duration of the fixed income portfolio stood at 1.9 years. As noted above, there was a change to the geographical allocation of the fixed income portion of the portfolio during the quarter as US bonds were sold from the overseas bond portfolio. Only 10% of the portfolio remains invested in overseas bonds, with 5% in Canada and 5% in Australia.

5.10 Newton

	2016			2015				2014	One	Two	Since Start
Newton	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**31/08/2012**
£57,981	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	**1.5**	4.3	4.0	1.5	(1.3)	(2.7)	4.4	0.9	11.3	6.3	5.0
Benchmark	**1.1**	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.4	4.4	4.5
Difference	**0.4**	3.2	2.9	0.4	(2.4)	(3.8)	3.3	(0.2)	6.9	1.9	0.5

Reason for appointment

Newton was appointed, with Pyrford, as the Fund's absolute return (AR) manager to act as a diversifier from equities. The manager has a fixed benchmark of one month LIBOR plus 4%. AR managers have a similar return compared to equity but are likely to underperform equity when markets increase rapidly and outperform equity when markets suffer a sharp fall. The years 2013 and 2014 could be classified as a significant market rally and therefore, in comparison to equities, Newton has underperformed.

Performance:
The Mandate generated a return more than its performance reference. Since the turn of the year and since initial funding, the Mandate has outperformed its return objective and has kept pace with global equities (in sterling terms), while managing to deliver reduced levels of volatility and demonstrating an impressive ability to preserve capital. The Mandate's exposure to gold made a positive contribution to performance.

The Mandate's positive return was also partly founded on strong performance by the government bond exposure. The exposure to global equities proved beneficial, with Novartis, CMS Energy, Wolters Kluwer and Merck making positive contributions. The Mandate's exposure to alternative assets, principally through UK infrastructure and renewable-energy assets, along with convertible bonds, also aided performance.

Activity:
Throughout the quarter Newton tactically traded the Mandate's exposure to long-duration US Treasuries, as well as utilising shorter-dated US Treasuries for cash management purposes. Following sustained strong performance Newton implemented put options on the US long bond future, and set up similar positions on the Euro-Bund future. Volatility during the quarter enabled Newton implement new positions in Dixons Carphone, Dong Energy and Samsung SDI.

Following strong performance Newton have rebalanced its gold exposure, taking profits from some of the gold-mining equities and increasing exposure to the physical metal.

Outlook and Strategy:
Newton believe that the prospect of a permanent loss of capital is more and more likely to occur. Newton continue to be cautiously positioned, using their proven ability to select securities to enable a much greater exposure to return-seeking assets with solid fundamental prospects, at much better valuation levels, enabling them to deliver returns over the long term.

5.11 BNY Standish

	2016			2015				2014	One	Two	Since Start
Standish	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Year**	**Years**	**20/08/2013**
£63,656	**%**	%	%	%	%	%	%	%	%	%	%
Actual Return	**1.4**	0.9	(1.9)	(1.4)	(2.7)	(1.5)	3.7	2.7	(1.0)	0.6	1.1
Benchmark	**1.1**	1.1	1.5	1.5	1.5	1.5	1.5	1.5	5.2	5.6	5.8
Difference	**0.3**	(0.2)	(3.4)	(2.9)	(4.2)	(3.0)	2.2	1.2	(6.2)	(5.0)	(4.7)

Reason for appointment

Standish were appointed to achieve a 6% total return from income and capital growth by investing in a globally diversified multi-sector portfolio of transferable fixed income securities including corporate bonds, agency and governments debt.

Performance

The US yield curve flattened over the quarter, with 10-year Treasury rates lower than two-year rates. The 10-year Treasury ended lower for the quarter. Spread sectors were mixed, while commercial mortgage-backed securities (CMBS) and asset-backed securities (ABS) were both weak, with each underperforming Treasuries. Despite the unexpected Referendum vote, US investment-grade corporate bond spreads were wider in September, which resulted in excess returns. High-yield bonds fell while emerging-market local currencies rose, and the S&P 500 was more or less unchanged on the quarter.

Outperformance in emerging-market currencies was offset by underperformance in developed-market currencies. While duration underweight in Japan and Europe underperformed, they were counterbalanced by overweight positions in South Korea, Canada, the US, Australia, Hungary, and Poland. Overall, the duration versus yield-curve positioning added during September. Asset allocation was slightly negative, with underperformance in investment-grade bonds and high-yield corporate bonds offset by outperformance in hard-currency emerging-market debt and ABS.

Outlook

The lack of a precedent to rely on for assessing the fallout for the UK or the global economy means the effect of the Referendum may not be known for some time; however, Standish believe the overall direct global economic consequences of the Referendum vote are likely to be limited. The UK's share of world GDP stood under 4% last year, and its bilateral trading relationships are mostly diversified by region and limited in scope.

Because of the referendum, Standish trimmed their 2016 forecast of the UK's real GDP growth. Standish believe the UK will avoid a recession because domestic demand, especially from households, provides a floor for growth.

Sterling is the asset most exposed to a vote to leave the EU. The BOE will undoubtedly monitor the situation closely but Standish does not expect a knee-jerk reaction. On balance, Standish believe the central bank is likely to leave the door open to an easier stance of monetary policy through dovish communication.

5.12 Currency Hedging

At the September Pension Panel Members received a presentation from Aon Hewitt on currency hedging within the Fund. Aon stated that sterling had seen considerable falls (13%) relative to the key currencies since the referendum on 23 June 2016 when the UK decided to leave the European Union. This had presented an opportunity for investors including pension schemes to hedge the currency of any non-GBP denominated investments, to benefit from the current low foreign exchange rate levels.

Members agreed to implement a currency hedge based placed on the passive strategy as outlined below:

i. 50% of the passive equity portfolio managed by UBS to be implemented when USD reaches $1.30 per GBP;
ii. 75% of the passive equity portfolio managed by UBS to be implemented when USD reaches $1.25 per GBP; and
iii. 100% of the passive equity portfolio managed by UBS to be implemented when USD reaches $1.20 per GBP.

On the 30th September 2016, a 50% hedge was placed on the Fund's passive equity holding with UBS. This hedge was placed at $1.29.

Subsequently a further 25% of the passive equity allocation was hedged on the 7th of October 2016. This hedge was placed at $1.29.

At this Panel Aon Hewitt will provide a verbal update on the Fund's currency positions.

6. Consultation

6.1 Council's Pension Fund monitoring arrangements involve continuous dialogue and consultation between finance staff, external fund managers and external advisers. The Strategic Director, Finance & Investment and the Fund's Chair have been informed of the approach, data and commentary in this report.

7. Financial Implications

Implications completed by: Jonathan Bunt, Strategic Director, Finance & Investment

7.1 The Council's Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. Investment decisions are taken based on a long-term investment strategy. The investment performance has a significant impact on the General Fund. Pensions and other benefits are statutorily calculated and are guaranteed. Any shortfall in the assets of the Fund compared to the potential benefits must be met by an employer's contribution.

7.2 This report updates the Panel on developments within the Investment Strategy and on scheme administration issues and provides an overview of the performance of the Pension Fund during the period.

8. Legal Implications

Implications completed by: Paul Feild, Senior Governance Solicitor

8.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.

8.2 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (SI 2009/3903) ("the 2009 Regulations") are the primary regulations that set out the investment framework for the Pension Fund. These regulations are themselves amended from time to time. The Regulations are made under section 7 of and Schedule 3 to the Superannuation Act 1972. They set out the arrangements which apply to the management and investment of funds arising in relation to a pension fund maintained under the Local Government Pension Scheme.

9. Other Implications

9.1 **Risk Management** - Investment decisions are taken based on a long-term investment strategy. Investments are diversified over several investment vehicles (equities – UK and overseas, bonds, property, infrastructure, global credit and cash) and Fund Managers to spread risk.

Performance is under constant review, with this focused on how the Fund has performed over the past three months, one year and three years.

Background Papers Used in the Preparation of the Report:

- WM Quarterly Q3 2016 Report; and
- Fund Manager Q3 2016 Reports.

List of appendices:

Appendix 1 - Fund Asset and Liability Values 31 March 2013 to 25 November 2016
Appendix 2 - Definitions
Appendix 3 - Roles and Responsibilities