

INVESTMENT MANAGEMENT REPORT

Report of the County Treasurer

All recommendations contained in this report are subject to confirmation by the Committee before taking effect.

Recommendations:

- (i) That the Investment Management Report be noted;
- (ii) That the Committee note compliance with the 2015/16 Treasury Management Strategy

1) FUND VALUE AND ASSET ALLOCATION

The table below shows the Fund value and the asset allocation for the Fund compared to the target asset allocation as at **31 March 2016**.

Fund Value and Asset Allocation

	Fund Value as at 31.3.16	Target allocation	Fund asset allocation at 31.3.16	Variation from Target
	£m	%	%	%
Fixed Interest				
Bonds	399.9	14.0	12.0	
Cash	47.4	2.0	1.4	
	447.3	16.0	13.4	-2.6
Equities				
Passive Equities	1,425.6	40.0	42.7	
Active Equities	470.6	15.0	14.1	
	1,896.2	55.0	56.8	+1.8
Diversified Growth Funds	486.1	15.0	14.6	-0.4
Alternatives				
Property	366.6	10.0	11.0	
Infrastructure	139.7	4.0	4.2	
	506.3	14.0	15.2	+1.2
Total Fund	3,335.9	100.0	100.0	

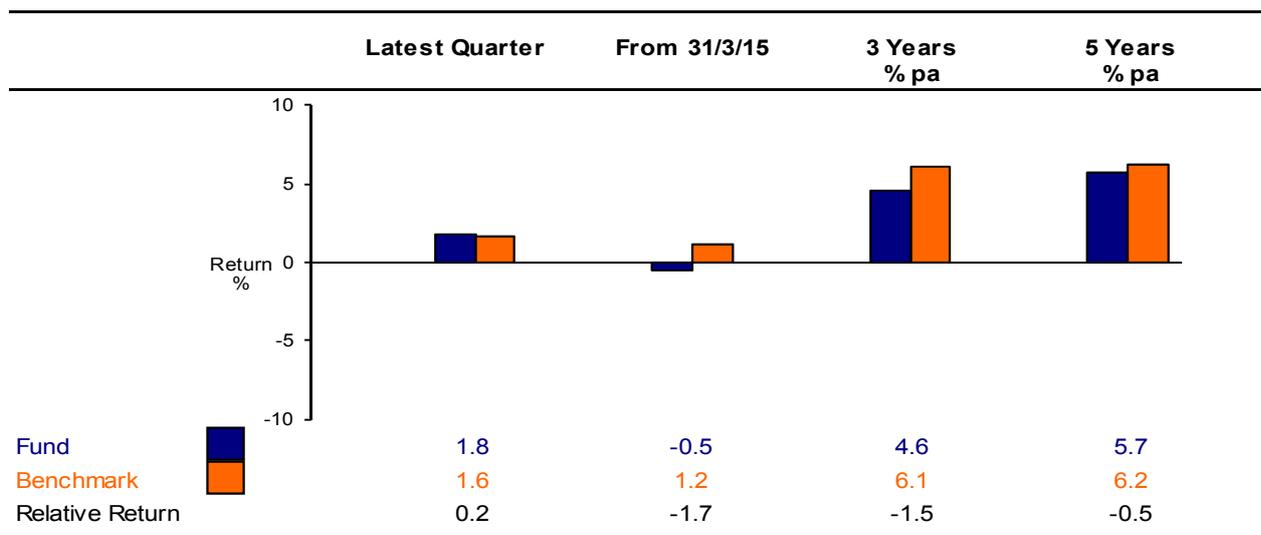
- The Fund value as at 31st March 2016 stood at £3,335.9 million, an increase of £26m over the quarter. However the fund value is still £38m (just over 1%) lower than at 31st March 2015.

- The Fixed Income allocation is being maintained below the target level for the time being, as agreed by the Committee at the meeting on 16th May 2014.
- All other asset classes are within 2% of the strategic asset allocation targets.

2) FUND PERFORMANCE

The performance of the Total Fund over the last quarter, the financial year to date, and on a rolling three and five year basis are shown in the following chart.

Longer Term Fund Performance Summary



The performance statistics quoted are net of fees for the current financial year, but the three year and five year figures shown combine gross performance up to 31 March 2014 and net of fees performance from 1 April 2014 onwards.

The year to 31 March 2016 has seen a negative absolute return of -0.5%. This is below the Fund benchmark of +1.2%. The return for the year is just below the average local authority pension fund return, and represents a 60th percentile ranking against the LGPS universe (i.e. 60% of funds performed better than the Devon fund and 40% had lower returns).

The below benchmark return for the year has also had an impact on the longer term figures. The rolling 3 year return is now 1.5% below benchmark, while the rolling 5 year return is below benchmark by 0.5%.

A breakdown of the performance of the Total Fund for the year to 31 March 2016 and the comparative Index returns are shown in the table below:

Performance for the nine months to 31 March 2016

Sector	Fund Return	Benchmark	Benchmark Description
	%	%	
Global Fixed Interest	1.5	2.3	BarCap Global Bonds
Cash (inc Foreign Currency)	0.4	0.3	GBP 7 Day LIBID
Passive Equities	-2.3	-2.5	Devon Bespoke Passive Index
Active Equities	-4.1	0.0	FTSE World
Diversified Growth Funds	-2.0	4.3	Devon Multi Asset Benchmark
Infrastructure	8.8	0.3	GBP 7 Day LIBID
Property	11.5	10.6	IPD UK PPF All Balanced Funds
Total Fund	-0.5	1.2	Devon Bespoke Index

Key issues over the year include:

- The negative absolute return largely reflects wider market conditions. Equity markets were broadly flat or slightly negative for the year. After a relatively positive April and May, equity markets lost considerable value between June and September, firstly as a result of the Greek debt crisis, and then concerns about the health of the Chinese economy. Although markets bounced back between October and December, it was not enough to make up the lost ground in the previous two quarters. The quarter to March also saw significant volatility at the beginning of the period, before moving back into positive territory. Negative returns on the Fund's assets will have an impact on our funding level.
- The diversified growth funds (DGFs) have underperformed their cash plus benchmarks over the period, and this contributed over half of the total fund underperformance. The DGFs will find it more difficult to achieve positive returns in negative markets, the key issue in relation to their performance is that they should preserve capital to a greater extent than the equity markets.
- Active equities have delivered a below benchmark return during the year (-4.1% against the FTSE World market return of 0.0%). Emerging markets continued to underperform developed markets, which detracted from returns, and the Fund's main global equities mandate continued to underperform. The specialist funds in combination were below benchmark, as a result of the allocation to emerging markets.
- The impact on the Passive Equities return of the active currency hedging strategy in relation to the overseas element of the investment has been positive against the US Dollar and the Japanese Yen, but negative against the Euro. The allocation to alternative indexation performed better than global market cap benchmarks.
- Global Fixed Interest was also below benchmark over the year, with the allocation to multi-sector credit not helping the position during a period where risk assets delivered negative returns.
- Property and infrastructure delivered a significant positive return over the period. Property continues to benefit from growth in UK GDP.

3) CASHFLOW AND CASH MANAGEMENT

- (a) The table below shows the balance between contributions received and due and the pension benefits paid out for the year to 31 March 2016, together with retained investment income and administrative and investment management costs. The retained investment income figure includes income from property, infrastructure and cash, but excludes all other investment income which is currently reinvested. The investment management costs only include manager fees where they are invoiced to the fund, and exclude fees which are deducted from the value of pooled funds as these do not involve a cash flow movement. The total figures for 2014/15 are shown for comparison.

Cashflow 2014/15 and 2015/16

	Income & Expenditure 2014/15	Income & Expenditure 2015/16
	£m	£m
Contributions Received/Due	150.9	153.3
Benefits Paid	(158.5)	(166.2)
Transfers In/Out *	0.3	(2.7)
Net New Money	(7.3)	(15.6)
Retained Investment Income	15.6	19.0
Management Expenses	(9.8)	(8.8)
Net Surplus Cash	(1.5)	(5.4)

* The transfers figure for 2014/15 excludes the £63.1m transfer to the Greater Manchester Pension Fund

- (b) The table shows a continuing picture of the benefits being paid exceeding the current contributions received. The gap is growing, but is still manageable within the current strategy.

4) TREASURY MANAGEMENT STEWARDSHIP 2015/16

- (a) At the February 2015 Committee, members approved a Treasury Management and Investment Strategy for 2015/16. This section of the report provides a review of the unallocated cash managed by the Investment Manager and his team during 2015/16.
- (b) Interest rates continue to be very low and the Bank of England base rate remained at 0.5% throughout the financial year. The rates available from the banks for call accounts and short term deposits have reduced during the year, largely as a result of regulatory issues designed to ensure the safety of bank deposits.
- (c) The Pension Fund maintains a very prudent approach to cash investments. Cash is now being maintained at a very low level, and therefore ensuring liquidity of the Fund's cash is a key requirement. Putting safety and liquidity before yield does however impact on the income being generated from these investments but is a necessary position to maintain.
- (d) At 31 March 2016 the unallocated cash on deposit amounted to **£21.3m**. The cash held is being maintained at a lower level than in the past, and it is therefore necessary to ensure its liquidity for cashflow purposes. Between August and February term deposits totalling £15m were made for periods of between 3 and 6 months pending drawdown of cash for the

Fund's remaining infrastructure investments. Much of this was drawn down in January, and at year end all cash was held in call accounts.

Cash on Deposit

Type of Deposit	Maturity period	Actual as at 31/03/15	Average Interest Rate	Current as at 31/03/16	Average Interest Rate
		£m	%	£m	%
Call and Notice Accounts	Immediate	30.3	0.50	21.3	0.41
Term Deposits	<30 Days	0.0		0.0	
	>30 Days	0.0		0.0	0.00
TOTAL (at 31st January 2016)		30.3	0.50	21.3	0.41

- (e) The weighted average rate being earned on cash deposits, as at 31 March 2016, was **0.41%**. This reflects the current low interest rate environment and the need to ensure liquidity as a result of the low level of cash being maintained.
- (f) The deposits in place during the year fully complied with the Fund's Treasury Management and Investment Strategy for 2015/16.

Mary Davis

Local Government Act 1972

List of Background Papers Nil

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