

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 2014/15 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 December 2014**.

Fund Value and Asset Allocation

| | Fund Value as at 31.12.14 | Target allocation | Fund asset allocation at 31.12.14 | Variation from Target |
|---------------------------------|---------------------------------|----------------------|-----------------------------------------|--------------------------|
| | £m | % | % | % |
| Fixed Interest | | | | |
| Bonds | 380.0 | 14.0 | 11.8 | |
| Cash | 62.7 | 2.0 | 1.9 | |
| | 442.7 | 16.0 | 13.7 | -2.3 |
| Equities | | | | |
| Passive Equities | 1,220.1 | 35.0 | 37.9 | |
| Interim Transition Fund | 174.0 | 5.0 | 5.4 | |
| Active Equities | 483.4 | 15.0 | 15.0 | |
| | 1,877.5 | 55.0 | 58.3 | +3.3 |
| Diversified Growth Funds | 478.1 | 15.0 | 14.8 | -0.2 |
| Alternatives | | | | |
| Property | 340.3 | 10.0 | 10.5 | |
| Infrastructure | 82.9 | 4.0 | 2.6 | |
| | 423.2 | 14.0 | 13.1 | -0.9 |
| Total Fund | 3,221.5 | 100.0 | 100.0 | |

- The Fund value as at 31st December 2014 stood at £3,221.5 million, a reduction of £11.9m over the last quarter. However this takes into account a transfer of £64.6m to the Greater

Manchester Pension Fund (GMPF) in relation to the restructuring of the Probation Service and transfer of all the associated liabilities.

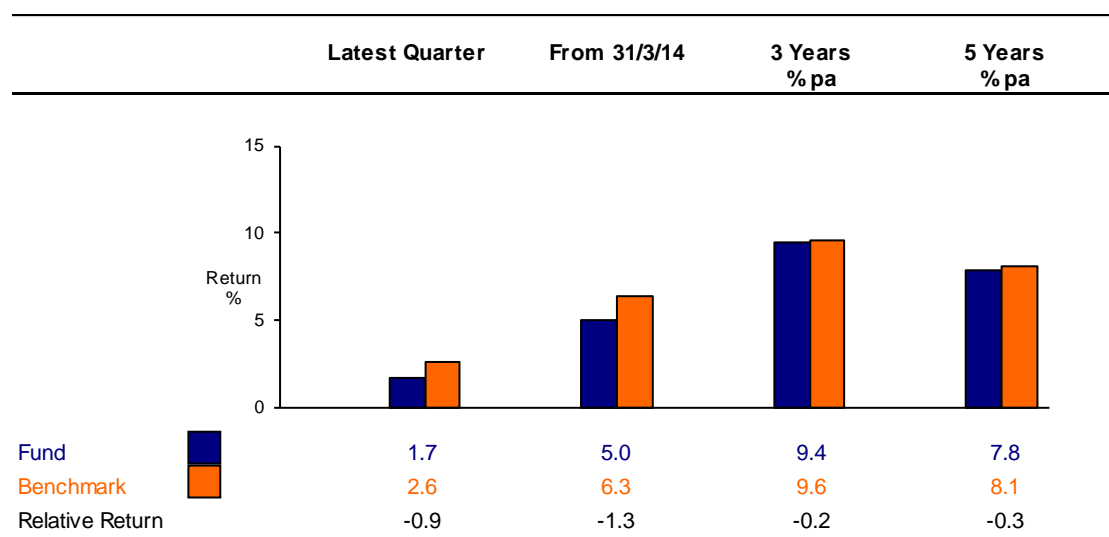
- The Fixed Income allocation is being maintained below the target level for the time being, as agreed by the Committee at the meeting on 16th May 2014.
- The transfer to GMPF was funded by the sale of equities, but the Fund's equity holdings remain above their target allocation of 55%. The allocation to equities will continue to remain over target as a result of the agreement to maintain fixed income at below the target level. However, further commitments to fund infrastructure will reduce the over-allocation to within 2.5% of the target allocation over the next 12 months. No additional action is proposed at this time.
- The agreed infrastructure commitments will bring the allocation to that asset class in line with the target allocation over the next 12 months.

2) FUND PERFORMANCE

WM Performance Services, who provide performance management statistics for the Fund are in the process of changing the basis of their approach to measure performance net of all fees. In the past performance figures have not taken account of invoiced fees, but have been net of underlying fees incurred directly within pooled funds. Due to the difficulties of backdating their approach performance will only be shown net of fees from 1 April 2014. Therefore the performance statistics quoted in this report will be net of fees for the current financial year, but the three year and five year figures shown will combine gross performance up to 31 March 2014 and net of fees performance from 1 April 2014 onwards. The impact on the current year figures will be to reduce the return at an overall fund level by around 0.2%

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



Relative performance over the quarter to 31 December was disappointing. The Fund return for the nine months was +5.0%, which was 1.3% below the Fund's customised benchmark. Over the longer term the rolling 3 year return is now showing a return of 0.2% below benchmark, while the rolling 5 year return is also below benchmark.

Key issues over the quarter include:

- The main reason for underperformance is the return on Active Equities which is significantly below benchmark. The active managers have performed poorly and the specialist funds also suffered as a result of the significant exposure to emerging markets and European small cap which have performed poorly.
- The impact on the Passive Equities return of the active currency hedging strategy in relation to the overseas element of the investment was less positive as a result of the strengthening of the US Dollar against Sterling over the quarter.
- Global fixed interest was below benchmark due to the negative performance of the multi-sector credit fund. Market conditions have been less favourable to the type of assets the multi-sector credit fund is invested in during the six months since the investment was made and this investment needs to be judged over a longer term.
- The diversified growth funds have outperformed their cash plus benchmarks.
- The strongest absolute return was on property, although the return was below the benchmark.

A breakdown of the performance of the Total Fund for the **nine months to 31 December 2014** and the comparative Index returns are shown in the table below:

Performance for the nine months to 31 December 2014

| Sector | Fund Return | Benchmark | Benchmark Description |
|-----------------------------|--------------------|------------------|-------------------------------|
| | % | % | |
| Global Fixed Interest | 3.2 | 5.0 | BarCap Global Bonds |
| Cash (inc Foreign Currency) | 6.1 | 0.3 | GBP 7 Day LIBID |
| Passive Equities | 4.9 | 4.8 | Devon Bespoke Passive Index |
| Active Equities | 2.4 | 10.5 | FTSE World |
| Diversified Growth Funds | 5.2 | 3.2 | Devon Multi Asset Benchmark |
| Infrastructure | 0.9 | 0.3 | GBP 7 Day LIBID |
| Property | 12.5 | 13.5 | IPD UK PPF All Balanced Funds |
| | | | |
| Total Fund | 5.0 | 6.3 | Devon Bespoke Index |

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 nine months to 31 December 2014, together with retained investment income and administrative and investment management costs. The total figures for the last financial year are shown for comparison. The 2013/14 figures are for the whole of the financial year, so will not be directly comparable to the nine month figures to December 2014, but the comparison illustrates the trend in terms of net new money and net surplus cash.

Cashflow 2013/14 and 2014/15 to 31 December 2014

| | Income & Expenditure 2013/14 | Income & Exp. to 31.12.14 |
|----------------------------|-----------------------------------------|--------------------------------------|
| | £m | £m |
| Contributions Received/Due | 149.0 | 109.0 |
| Benefits Paid | (150.5) | (118.7) |
| Transfers In/Out * | 1.2 | (0.1) |
| Administration Expenses | (2.0) | (1.5) |
| Net New Money | (2.3) | (11.3) |
| | | |
| Retained Investment Income | 14.1 | 11.8 |
| Investment Mgt Expenses | (8.0) | (6.0) |
| | | |
| Net Surplus Cash | 3.8 | (5.5) |

* The transfers figure excludes the £64.6m transfer to the Greater Manchester Pension Fund

- (b) The table shows a continuing picture of the benefits being paid exceeding the current contributions received. For the first nine months of the 2014/15 financial year the deficit, added to the cost of investment management, has not been balanced out by the addition of retained investment income from the property mandate, infrastructure and the in-house managed cash, but the difference is manageable in the short term within current cash resources.
- (c) At 31 January 2015 the unallocated cash on deposit amounted to **£37.2m**. Members will note from the table below that all the cash is now held in Call Accounts. 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. This has an impact on the rates achievable.

Cash on Deposit

| Type of Deposit | Maturity period | Actual as at 31/03/14 | Interest Rate | Current as at 31/01/15 | Interest Rate |
|-------------------------------------|------------------------|------------------------------|----------------------|-------------------------------|----------------------|
| | | £m | % | £m | % |
| Call and Notice Accounts | Immediate | 29.2 | 0.65 | 37.2 | 0.48 |
| | | | | | |
| Term Deposits | <30 Days | 5.8 | 0.85 | 0.0 | |
| | | | | | |
| | >30 Days | 0.0 | | 0.0 | |
| | | | | | |
| TOTAL (at 31st January 2015) | | 35.0 | 0.68 | 37.2 | 0.48 |

- (d) The weighted average rate being earned on cash deposits, as at 31 January 2015, is **0.48%**. 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. The deposits in place fully comply with the Fund's Treasury Management and Investment Strategy for 2014/15.

Mary Davis

Local Government Act 1972

List of Background Papers Nil

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