BROMLEY CIVIC CENTRE, STOCKWELL CLOSE, BROMLEY BRI 3UH

THE LONDON BOROUGH
www.bromley.gov.uk

TELEPHONE: 020 8464 3333
CONTACT: Keith Pringle
keith.pringle@bromley.gov.uk

DIRECT LINE: 020 8313 4508
FAX: 020 8290 0608

DATE: 13 February 2015

To: Members of the
PENSIONS INVESTMENT SUB-COMMITTEE

Councillor Simon Fawthrop (Chairman)
Councillor Alan Collins (Vice-Chairman)
Councillors Eric Bosshard, Peter Fookes, David Livett, Russell Mellor and Neil Reddin FCCA

Glenn Kelly (Non-Voting Staff Representative)

A meeting of the Pensions Investment Sub-Committee will be held at Bromley Civic Centre on **TUESDAY 24 FEBRUARY 2015 AT 7.30 PM**

MARK BOWEN
Director of Corporate Services

Copies of the documents referred to below can be obtained from http://cds.bromley.gov.uk/

A G E N D A

1 **APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS**

2 **DECLARATIONS OF INTEREST**

3 **CONFIRMATION OF MINUTES OF THE MEETINGS HELD ON 2ND DECEMBER 2014 AND 3RD FEBRUARY 2015 EXCLUDING THOSE CONTAINING EXEMPT INFORMATION** (Pages 3 - 14)

4 **QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING**

In accordance with the Council's Constitution, questions to this Committee must be received in writing four working days before the date of the meeting. Therefore please ensure that questions are received by the Democratic Services Team by 5pm on Wednesday 18th February 2015.

5 **PENSION FUND PERFORMANCE Q3 2014/15** (Pages 15 - 34)

6 **PENSION FUND - INVESTMENT REPORT**

Printed copies of reports from the Council's Fund Managers are circulated to Sub-Committee Members with this agenda. Representatives of Blackrock and MFS will be attending the meeting for this item.

7 REVISED INVESTMENT STRATEGY - PHASE 3 (Pages 35 - 44)

8 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

The Chairman to move that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

	Items of Business	Schedule 12A Description
9	**CONFIRMATION OF EXEMPT MINUTES OF THE MEETING HELD ON 2ND DECEMBER 2014** (Pages 45 - 46)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)

....

PENSIONS INVESTMENT SUB-COMMITTEE

Minutes of the meeting held at 7.30 pm on 2 December 2014

Present

Councillor Simon Fawthrop (Chairman)
Councillor Alan Collins (Vice-Chairman)
Councillors Eric Bosshard, Peter Fookes, David Livett, Russell Mellor and Neil Reddin FCCA

Also Present

Alick Stevenson, AllenbridgeEpic Investment Advisers

12 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

There were no apologies.

13 DECLARATIONS OF INTEREST

Councillor Russell Mellor declared a personal interest by virtue of receiving a Pension from the Local Government Pension Scheme.

Councillor Eric Bosshard declared a personal interest as a former Member of the Local Government Pension Scheme.

14 CONFIRMATION OF MINUTES OF THE MEETING HELD ON 19TH AUGUST 2014 EXCLUDING THOSE CONTAINING EXEMPT INFORMATION

The minutes were agreed.

Members were also updated on certain matters.

In view of concerns related to the position of a number of Local Government Pension Schemes, and in the context of local decision making, it was suggested that an expected Government announcement might highlight an intention to require Local Authorities to take a passive investment approach for their pension funds. Such an approach was currently encouraged by Government.

Concerning proposals for Local Pension Boards, final Government guidance was awaited. There might be an option for two Local Authorities to join together to provide a Pension Board. Pension Board arrangements for L B Bromley would need to be agreed at Full Council on 23rd February 2015 and the Sub Committee would meet beforehand to consider proposals. Although a Local Pensions Board was expected to provide scrutiny, its need was questioned as a significant check/balance is already provided by a Fund's Actuary.

In relation to L B Bromley's Shadow Pension Fund, comprising £2.7m of the £10m allocated to Diversified Growth investment, any earnings or capital value changes on the £2.7m would be added to the earmarked reserve that had been set up.

For the Collaborative Investment Vehicle (CIV) proposed for boroughs by London Councils, some authorities had yet to commit to the initiative including L B Bromley.

15 QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING

There were no questions.

16 PENSION FUND PERFORMANCE Q2 2014/15

Report FSD14076

Report FSD14076 provided details of investment performance for Bromley's Pension Fund in the 2nd quarter of 2014/15. More detail was provided in an appended report from the Fund's Investment Adviser including commentary on developments in financial markets, their impact on the Council's Fund, and future outlook.

Information on general financial and membership trends of the Pension Fund was also outlined along with summarised information on early retirements. Financial information included historic data on the fund's value, previous allocations to fund managers, distributions of surplus revenue fund cash to fund managers, and movements in the value of the FTSE 100 index. Baillie Gifford also provided commentary on their performance and a view on economic outlook. Baillie Gifford representatives attended to discuss performance, economic outlook/prospects, and other matters concerning the portfolios under Baillie Gifford management.

Quarterly reports from all fund managers had been circulated to Sub-Committee Members with the meeting agenda.

At 30th September 2014 the fund value stood at £655.9m (and by 19th November 2014 this had risen to £688.8m). Overall, the fund returned +3.0% in the second quarter matching the benchmark return. This performance was in the 7th percentile of the local authority average.

Medium and long-term, the fund's returns have remained particularly strong, achieving overall local authority average rankings in the 29th percentile for 2013/14 and the 4th percentile for 2012/13 (the fund being subject to transition and change in both years).

In noting the fund's value, it was suggested the fund was not performing significantly better than the FTSE 100 Index. However, returns were helping to reduce the funding gap and passive investments would provide the necessary income. Returns were fed into the Pension Fund Revenue Account and amounts outstanding after funding liabilities were directed back into the Fund for investment. As such it was not possible to identify specific details of such returns as they are automatically re-invested and the need for a separate Pension Fund a/c to hold the re-investment sums was not considered necessary. There were also costs related to establishing a separate account. The actuarial target for overall returns to meet fund liabilities stood at 5.6% and the current level of returns should help reduce the fund deficit. It was also suggested that equivalent figures be provided for previous years to show a trend (seasonal comparisons).

It was also noted there would be fewer employees in the future and a reduced level of contributions. It would not be possible to take the same level of risk for the future as in previous years, the fund now technically having a negative cash flow, excluding returns from equities (these returns being re-invested back into the fund). It was also possible for employees to take pension benefits at age 55 and a cash flow problem could arise should there be a significant demand for early pensions. It might be necessary in future to merge with another pension fund having a positive cash flow to help meet liabilities. The level of employee contributions had also decreased in accordance with Government regulation.

RESOLVED that the report be noted.

17 PENSION FUND - INVESTMENT REPORT

In their presentation to the Sub-Committee, Baillie Gifford highlighted the valuations of their three portfolios – Global Alpha (global equities), Diversified Growth, and Fixed income – as at 30th November 2014, in comparison to valuation of the Portfolios at 30th September 2014.

For the Diversified Growth Portfolio, Baillie Gifford's objective was to outperform UK base rate by at least 3.5% per annum (net of fees) over rolling five year periods with an annualised volatility of less than 10% over the same periods. On performance to 30th September 2014 for Diversified Growth funds, Baillie Gifford had achieved a net return for the fund of 6% per annum since inception, outperforming the UK base rate by 4%. The presentation also highlighted the performance of Baillie Gifford's Diversified Growth Pension Fund between 31st December 2008 and 30th September 2014 to illustrate a positive performance delivered with low volatility. Performance attribution and commentary on certain DGF asset classes in the 12 months to 30th September 2014 was also outlined, with an indication that the fund returned 7.8% gross of fees over the year. In discussion the impact of fees was outlined to Members. It was also noted that the Active Currency asset class had delivered a return of 1.3%. In theory it was possible to lose money on any one of the asset classes but the involvement of research was highlighted and currency as an asset class was suited to Baillie Gifford's investment approach. Overall performance of economies was the ultimate driver and a difference could be made over the long term. It was explained that a typical holding period by Baillie Gifford for a currency asset was six months rather than have a short term approach to the asset class. In terms of outlook for the future, Baillie Gifford was encouraged by improvements in economic data in parts of the developed world and improving fundamentals gave grounds for optimism. However, Baillie Gifford felt that risks remained. It was felt that the end of Quantative Easing (QE) and increase in interest rates might have a negative impact on higher yielding assets. The US in particular was curtailing its use of QE although it was suggested to Members that the extent of QE across other parts of the world could rise, with Europe in particular increasing QE.

Further detail on Baillie Gifford's Diversified Growth Fund Portfolio was appended to the presentation. This included details of asset types the Fund invests in, asset class returns within the fund, and asset attribution. The portfolio continued to be invested across a broad range of asset classes. There were substantial allocations to more defensive asset classes e.g. cash, investment grade bonds and structured finance. Baillie Gifford remained confident that the fund could deliver a worthwhile return in a range of environments. Returns had been supported by improving economic factors with most asset classes performing well. However, the pace of recovery remained modest, continuing to diverge across regions. Emerging market assets experienced sharp falls early during the 12 months to 30th September 2014, with some recovery in recent months.

However, on expectations for long term return, a number of assets looked to offer higher than average ten year expected returns against cash; Baillie Gifford continued to expect a particularly low return on cash. Nominal returns and returns relative to inflation were likely to be lower than average across all asset classes. Equity valuations were higher than 12 months previously, hence a lower return expectation. This also applied to a lesser extent for infrastructure, high yield credit, and insurance-linked allocations. Government bonds, investment grade bonds and emerging market bonds were on lower valuations.

It was noted that some 13% of the Diversified Growth fund was allocated to Emerging Market Bonds, including exposure in Mexico, Peru and Columbia. It was explained that Baillie Gifford focused on companies rather than countries, considering how companies can grow their earnings. For Mexico there was a new Government and the US was more confident. There appeared to be keenness on re-structures and the largest trading partner for Mexico was the US. Longer term Bonds issued by emerging market countries (in their local currencies) could be expected to achieve a real return of 2% over cash. However, risks varied by country and there was a limited correlation to equities. On a nearer term view, the current index yield at 6.4% was attractive. However certain countries were struggling with current account deficits and some selectivity amongst countries was appropriate. The purchase of the Baillie Gifford Emerging Market Bond Fund had been implemented and there was selective additional exposure to stronger economies.

It was noted that the Bromley Pension Fund could go cash negative in a further five to six years. It was explained that the Diversified Growth Fund aimed to beat base rates and there was a strong absolute return over the medium term. Diversified Growth was a better strategy. For Treasury Management, there would be no intention to invest in equity. Treasury management was different and it was necessary to rely on fund managers taking a long term approach.

Concerning Baillie Gifford's Global Alpha strategy focusing on long term global equity, this was described as "bottom up stock picking", well diversified and with a low turnover. The objective was to outperform the MSCI All Country World Index by 2 – 3% p.a. (before fees) over rolling five year periods. As at 30th November 2014 the Portfolio Value stood at £230,177,343 and the portfolio had returned 4.8% (gross of fees) since inception on 31st December 2013 against a benchmark of 6.4%. The intention was to hold investments in the portfolio for about five years to see real benefit. Details of the top ten stock contributors were provided for the portfolio along with the bottom ten stock contributors. A brief update was provided on Baillie Gifford's research related to the portfolio and the composition of the portfolio by stock holding.

Noting that Baillie Gifford's objective to outperform the MSCI All Country World Index by 2 – 3% p.a. over rolling five year periods was before fees, Members asked that the objective also be provided net of fees. As such Baillie Gifford was happy to provide performance figures gross of fees and net of fees. It was suggested that net of fees the return would change from 4.8% to about 4.5%. It was also explained that the actuarial assumption is long term and for actuarial purposes the expectation of return is about 7% per annum.

The presentation document included details of Baillie Gifford's investment philosophy for the Global Alpha portfolio along with a summary of the investment process. Growth profiles were also provided according to Stalwart, Rapid, Cyclical and Latent types with particular company characteristics attributed to each growth profile type. An outline of Global Alpha activity in companies identified new buys, additions, complete sales and reductions. The top ten holdings were highlighted as were sector weights and regional weights. A Global Alpha list of stock holdings identified the percentage holding in various stock as at 30th September 2014.

Concerning Bailie Gifford's Fixed Income Portfolio, this had an objective to outperform 50% Gilt / 50% Corporate Bond benchmark by 1.5% p.a. over rolling three year periods. The value of the Portfolio at 30th September 2014 stood at £48,144,437. Baillie Gifford's fixed income approach was outlined in respect of Corporate Bonds (bottom-up credit analysis), Government Bonds (Global approach covering interest rates and currencies) and Asset Allocation (Government versus credit – selective investment in high yield and emerging market bonds). The Fixed Income portfolio had achieved a return of 9% against a benchmark of 7% to 30th September 2014 from its inception on 9th December 2013. In terms of general outlook for Fixed Income the presentation advised that long term interest rates might not return to previous average levels in view of factors such as lower trend economic growth, ageing populations and excess global savings. In the short term, interest rates were influenced by continuing loose central bank policy. It was felt that yields might be lower for some time. In regard to Corporate Bonds, Baillie Gifford also felt that there were overweight securitised bonds with real assets. Reference was also made to underweight banks. On Government bonds, it was felt that yields were too high in some emerging markets; Baillie Gifford was also positioned to benefit from falling Eurozone inflation. Regarding currency, Baillie Gifford favoured recovering economies such as the U.S. and Mexico.

In view of the UK Government looking to provide the Scottish Parliament with increased tax raising powers and anticipating any possible increase to personal taxation rates in Scotland, the Chairman enquired whether there might be a risk of Bailie Gifford losing key personnel as a result. Additionally the Chairman enquired whether there might also be a risk that the Scottish Government might raise increased company tax levies on Bailie Gifford. It was explained that VAT continued to be controlled by the UK Government and Baillie Gifford had a keen focus on people in its business. There was a low turnover of staff. It was suggested there is only some 18,000 in Scotland paying the higher tax rate of 45%. Higher rate earners in the company could potentially have to pay a 50% tax rate were income tax levels to rise to that extent but the company would impress upon the Scottish Government that it would be foolhardy to make Scotland uncompetitive through such levels of taxation.

RESOLVED that in the context of Baillie Gifford's Global Alpha strategy, Baillie Gifford provide performance returns (i) gross of fees and (ii) net of fees.

18 REVISED INVESTMENT STRATEGY - PHASE 3

Report FSD14077

Members considered a report which included information related to illiquid fixed income assets, potentially part of the 20% protection allocation under Phase 3 of the investment strategy.

An update from the Fund's Investment Advisers, AllenbridgeEpic was appended to Report FSD14077. A copy of the Advisers' paper on Options for Phase 3 of the Investment Strategy (Fixed Income), as presented to the Sub Committee's previous meeting, was also appended to the report.

An approach for funding any new investments was covered in a further appendix to the report provided under Part 2 of the agenda. In view of this and the likelihood of discussions on the report involving exempt information, it was agreed to move consideration of this item to Part 2 of the agenda.

19 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

RESOLVED that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

The following summaries
refer to matters
involving exempt information

20 REVISED INVESTMENT STRATEGY - PHASE 3

Report FSD14077

Members considered what investment approach (or otherwise) should be taken in regard to illiquid fixed income assets as any potential part of the 20% protection allocation under Phase 3 of the investment strategy.

The Meeting ended at 9.53 pm

Chairman

This page is left intentionally blank

PENSIONS INVESTMENT SUB-COMMITTEE

Minutes of the meeting held at 7.00 pm on 3 February 2015

Present:

Councillor Simon Fawthrop (Chairman)
Councillor Alan Collins (Vice-Chairman)
Councillors Eric Bosshard, Peter Fookes, David Livett, Russell Mellor and Neil Reddin FCCA

Also Present:

Councillor Graham Arthur

21 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

There were no apologies for absence.

22 DECLARATIONS OF INTEREST

There were no declarations of interest.

23 LOCAL PENSION BOARD

Report FSD15013

The Sub-Committee considered a report outlining proposed changes to the structure and governance arrangements of Local Government Pension Schemes (LGPS) brought about by the Public Service Pensions Act 2013 and associated Regulations and seeking the required approvals for the establishment of a Local Pension Board. Final regulations and guidance had since been issued and a supplementary paper was circulated setting out the latest position, although further information was still awaited. The most fundamental change was that the regulations now allowed for a Local Pension Board to be combined with an existing Committee, subject to the approval of the Secretary of State. If Bromley were to submit an application for a Combined Board which was approved then the Local Pension Board would be disbanded. Officers advised that the criteria and associated conditions were still awaited but it might be possible to establish a Combined Board with General Purposes and Licensing Committee. However, it was likely that there would be complications involved in this approach and it might require the membership of the Committee to be reviewed to ensure that the requirements of the Regulations were met. The key was to secure approval for a Local Pension Board in line with the statutory timescales for its establishment and then consider whether a Combined Board would provide a suitable alternative arrangement once further information became available.

The Sub-Committee considered that the establishment of a Local Pension Board was completely unnecessary for an authority that already ran its pension scheme effectively, with existing good governance and in an open and transparent way, but they were advised that it was a statutory requirement. As a minimum, the Board had to comprise four people (two employer representatives and two scheme member representatives) who had to have the capacity to represent employers and members respectively. Generally, it was for the Administering Authority to determine the detailed remit and terms of reference of the Board in accordance with the Regulations. It was proposed that the Board would meet twice a year and produce an annual report, but the Sub-Committee considered that it should meet only once a year supported by attendance at Sub-Committee meetings.

Members were concerned that the costs of the proposed Local Pension Board should be minimised and were informed that any legal, financial or other advice or support would normally come from existing internal Council resources. The Sub-Committee supported the proposal that Board Members would not be paid an allowance but would be reimbursed for reasonable expenses incurred. Individual Board Members had certain personal responsibilities and legal obligations and enquiries were under way to ensure that they would be adequately covered through the Council's existing insurance arrangements, but Members noted that this could not cover reputational risk.

RESOLVED that

(1) The Pensions Investment Sub-Committee having considered the report notes and agrees the recommendations subject to writing to the Secretary of State as follows:-

This Sub-Committee views the introduction of Pension Boards in local authorities such as Bromley Council causes duplication, both an additional layer of bureaucracy and additional unwanted extra costs, at a time of reduced budgets.

This is demonstrated by Bromley's

1) **open and transparent meetings, minutes and agenda of which are published on line;**

2) **the ability for members of the public, concerned parties and members of the LGPS to ask questions in writing or in person at meetings;**

3) **the inclusion of a union representative attending the Sub-Committee;**

4) **a reporting structure that gives additional opportunities for scrutiny at both the parent Committee and at full Council.**

5) notes that the Pensions Fund and Sub-Committee are also independently audited as part of the Authority's good governance process.

We would therefore urge the Secretary of State to remove this additional burden by allowing local Authorities with a good governance scheme to opt out of the need for a Local Pensions Board.

(2) General Purposes and Licensing Committee recommend that Council

(i) approve the establishment of a Local Pension Board;

(ii) approve the composition of the Local Pension Board as set out in paragraph 3.17 of the report;

(iii) approve the draft terms of reference (appendix 2 to the report), subject to incorporating the following amendments –

- **the Board should meet once a year;**
- **in the event of non-attendance, membership will be reviewed (amended from consistent non-attendance);**
- **clarifying the process for the replacement of Board members who die in office;**
- **Board Members will be invited to attend meetings of the Pensions Investment Sub-Committee.**

(iv) delegate authority to the Director of Finance, in consultation with the Chairman of Pensions Investment Sub-Committee and the Chairman of General Purposes and Licensing Committee to make any agreed changes to the draft terms of reference as set out in paragraph 3.18 of the report;

(v) agree the process for nominations and appointments as set out in paragraphs 3.22 and 3.23 and that:

(a) appointment of the two employer representatives be made by Council;

(b) appointment of the two member representatives be formally delegated to the General Purposes and Licensing Committee on the recommendation of an appointments panel as constituted in paragraph 3.23 and in the terms of reference;

(vi) delegate authority to the Director of Finance, in consultation with the Chairman of Pensions Investment Sub-Committee and the Chairman of General Purposes and Licensing Committee, to

make any changes necessary arising from the issue of final Regulations;

(vii) on the basis that it would provide a suitable alternative arrangement, in consultation with the Chairman of Pensions Investment Sub-Committee and the Chairman of General Purposes and Licensing Committee, authorise the Director of Finance to make an application to the Secretary of State for approval to establish a Combined Local Pension Board and Committee subject to any criteria or conditions that may be applied;

(viii) agree that, should such an application be successful, the Local Pension Board be disbanded and the establishment of a Combined Board be subject to a further report setting out the proposed structure and terms of reference.

The Meeting ended at 7.57 pm

Chairman

Report No.
FSD15012

London Borough of Bromley

PART 1 - PUBLIC

Decision Maker:	**Pensions Investment Sub-Committee**
Date:	**24th February 2015**
Decision Type:	Non-Urgent Non-Executive Non-Key
Title:	**PENSION FUND PERFORMANCE Q3 2014/15**
Contact Officer:	Martin Reeves, Principal Accountant (Technical & Control) Tel: 020 8313 4291 E-mail: martin.reeves@bromley.gov.uk
Chief Officer:	Director of Finance
Ward:	All

1. Reason for report

This report includes a summary of the investment performance of Bromley's Pension Fund in the 3rd quarter of 2014/15. More detail on investment performance is provided in a separate report from the Fund's external advisers, AllenbridgeEpic, which is attached as Appendix 5. Representatives of Blackrock and MFS, having now completed their first year as our Pension Fund managers, will be present at the meeting to discuss performance, economic outlook/prospects and other matters relating to their portfolios. One of the other fund managers, Baillie Gifford, has provided a brief commentary on its performance and on its view of the economic outlook and this is attached as Appendix 2. The report also contains information on general financial and membership trends of the Pension Fund and summarised information on early retirements.

RECOMMENDATION

The Sub-Committee is asked to note the report.

Corporate Policy

1. Policy Status: Existing policy. The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2013, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

2. BBB Priority: Excellent Council.

Financial

1. Cost of proposal: No cost

2. Ongoing costs: Recurring cost. Total administration costs estimated at £2.5m (includes fund manager/actuary/adviser fees, Liberata charge and officer time)

3. Budget head/performance centre: Pension Fund

4. Total current budget for this head: £35.8m expenditure (pensions, lump sums, etc); £38.6m income (contributions, investment income, etc); £693.7m total fund market value at 31st December 2014)

5. Source of funding: Contributions to Pension Fund

Staff

1. Number of staff (current and additional): 0.4 FTE

2. If from existing staff resources, number of staff hours: c 14 hours per week

---

Legal

1. Legal Requirement: Statutory requirement. Local Government Pension Scheme (LGPS) Regulations 2013

2. Call-in: Call-in is not applicable.

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 5,637 current employees; 4,937 pensioners; 5,007 deferred pensioners as at 31st December 2014

Ward Councillor Views

1. Have Ward Councillors been asked for comments? No.

2. Summary of Ward Councillors comments: N/A

3. COMMENTARY

Fund Value

3.1 The market value of the Fund ended the December quarter at £693.7m (£655.9m as at 30th September 2014) and, by the end of January 2015, it had risen further to £714.9m. The comparable value as at 31st December 2013 was £618.8m. Historic data on the value of the Fund are shown in a table and in graph form in Appendix 1.

Performance targets and investment strategy

3.2 Historically, the Fund's investment strategy has been broadly based on a high level 80%/20% split between growth seeking assets (representing the long-term return generating part of the Fund's assets) and protection assets (aimed at providing returns to match the future growth of the Fund's liabilities). Between 1998 and 2012, Baillie Gifford and Fidelity managed balanced mandates along these lines. This strategy was confirmed in 2012, following a comprehensive review of the Fund's investment strategy. This review concluded that the growth element would, in future, comprise a 10% allocation to Diversified Growth Funds (DGF) and a 70% allocation to global equities. The latter eliminated our previous arbitrary regional weightings and provided new managers with greater flexibility to take advantage of investment opportunities in the world's stock markets, thus, in theory at least, improving long-term returns. A 20% protection element would remain in place for investment in corporate bonds and gilts.

3.3 It was agreed that this would be implemented in three separate phases and, following presentations by a short-list of four prospective managers to the meeting in November 2012, Phase 1 was implemented on 6th December 2012 with a transfer of £50m from Fidelity's equity holdings (£25m to each of the two successful companies, Baillie Gifford and Standard Life).

3.4 Following further presentations by four prospective managers to a special meeting in November 2013, Phase 2 was implemented on 20th December 2013, with £200m being allocated to Baillie Gifford (from within their former equities holdings), £120m to MFS International (transferred from Fidelity) and £120m to Blackrock (£70m from Baillie Gifford and £50m from Fidelity). A report elsewhere on the agenda looks further at options for Phase 3 of the revised investment strategy.

Summary of Fund Performance

3.5 <u>Performance data for 2014/15 (short-term)</u>
A detailed report on fund manager performance in the quarter ended 31st December 2014 is provided by the fund's external adviser, AllenbridgeEpic, in Appendix 5. In overall terms, the total fund returned +5.6% (net of fees) in the latest quarter, compared to the overall benchmark return of +4.3%. This followed overall returns of +3.0% in the September quarter (benchmark also +3.0%) and +1.6% in the June quarter (benchmark +2.3%). With regard to the local authority average, the fund's performance in the December quarter was in the 6th percentile (the lowest rank being 100%). In the September quarter, Bromley's Fund was in the 8th percentile and, in the June quarter, it was in the 81st percentile. The June quarter was only the second full quarter since some 70% of the total assets of the Fund was moved (in December 2013) from the previous balanced mandates into new global equity mandates and it is perhaps reasonable to assume that this was, partly at least, due to the new managers "bedding in". In local authority average terms, the performance in the last two quarters has been very good.

3.6 <u>Medium and long-term performance data</u>
Since 2006, the WM Company has measured the fund managers' results against their strategic benchmarks, although, at total fund level, it continues to use the local authority indices and averages. Other comparisons with local authority averages may be highlighted from time to time to demonstrate, for example, whether the benchmark itself is producing good results. The Fund's medium and long-term returns have remained very strong. In spite of both 2012/13 and 2013/14

being years of transition and change, the Fund as a whole achieved overall local authority average rankings in the 29th percentile in 2013/14 and in the 4th percentile in 2012/13. For comparison, the rankings in earlier years were 74% in 2011/12, 22% in 2010/11, 2% in 2009/10 (the second best in the whole local authority universe), 33% in 2008/09, 5% in 2007/08, 100% in 2006/07 (equal worst in the whole local authority universe), 5% in 2005/06, 75% in 2004/05, 52% in 2003/04, 43% in 2002/03 and 12% in 2001/02. The following table shows the Fund's long-term rankings in all financial years back to 2004/05 and shows the medium to long term returns for periods ended on 31st December 2014 (in the 9th percentile for one year, in the 4th percentile for three years, in the 15th percentile for five years and in the 8th percentile for ten years). The medium to long-term results have been very good and have underlined the fact that the Fund's performance has been consistently strong over a long period.

Year	Whole Fund Return	Benchmark Return	Local Authority average	Whole Fund Ranking
	%	%	%	
Figures to 31/12/14				
1 year (1/1/14 to 31/12/14)	12.1	10.9	8.1	9
3 years (1/1/12 to 31/12/14)	14.6	12.3	11.0	4
5 years (1/1/10 to 31/12/14)	10.9	9.4	8.9	15
10 years (1/1/05 to 31/12/14)	9.8	8.3	7.5	8
Financial year figures				
2013/14	7.6	6.2	6.4	29
2012/13	16.8	14.0	13.8	4
2011/12	2.2	2.0	2.6	74
3 year ave to 31/3/14	***8.7***	***7.2***	***7.5***	***19***
2010/11	9.0	8.0	8.2	22
2009/10	48.7	41.0	35.2	2
5 year ave to 31/3/14	***15.8***	***13.4***	***12.7***	***3***
2008/09	-18.6	-19.1	-19.9	33
2007/08	1.8	-0.6	-2.8	5
2006/07	2.4	5.2	7.0	100
2005/06	27.9	24.9	24.9	5
2004/05	10.6	11.7	11.7	75
10 year ave to 31/3/14	***9.6***	***8.3***	***7.8***	***2***

Fund Manager Comments on performance and the financial markets

3.7 Baillie Gifford have provided a brief commentary on recent developments in financial markets, their impact on the Council's Fund and the future outlook. This is attached as Appendix 2.

Early Retirements

3.8 Details of early retirements by employees in Bromley's Pension Fund in the current year and in previous years are shown in Appendix 3.

Fund Manager attendance at meetings

3.9 At the August meeting, a programme of fund manager attendance was agreed and Baillie Gifford, who currently manage three separate portfolios (global equities, DGF and fixed income) attended the December meeting to discuss performance and other matters. Blackrock and MFS (global equity managers who have both just completed their first year of management) are attending this meeting and Fidelity (fixed income) and Standard Life (DGF) will attend the meeting on 19th May 2015.

4. POLICY IMPLICATIONS

4.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2013, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the established categories of investments, e.g. equities, bonds, property, etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

5.1 Details of the actual position of the 2014/15 Pension Fund Revenue Account (as at 31st December 2014) are provided in Appendix 4 together with fund membership numbers. A net surplus of £2.5m (including £5.1m investment income) was achieved in the first three quarters of 2014/15 and total membership numbers rose by 646. The overall proportion of active members has, however, declined in recent years and has fallen slightly from 36.4% at 31st March 2012 to 36.2% at 31st December 2014.

6 LEGAL IMPLICATIONS

6.1 The statutory provisions relating to the administration of the Local Government Pension Scheme are contained in the Local Government Pension Scheme (LGPS) Regulations 2013.

Non-Applicable Sections:	Personnel Implications
Background Documents: (Access via Contact Officer)	Analysis of portfolio returns (provided by WM Company). Monthly and quarterly portfolio reports of Baillie Gifford, Blackrock, Fidelity, MFS and Standard Life. Quarterly Investment Report by AllenbridgeEpic

Appendix 1

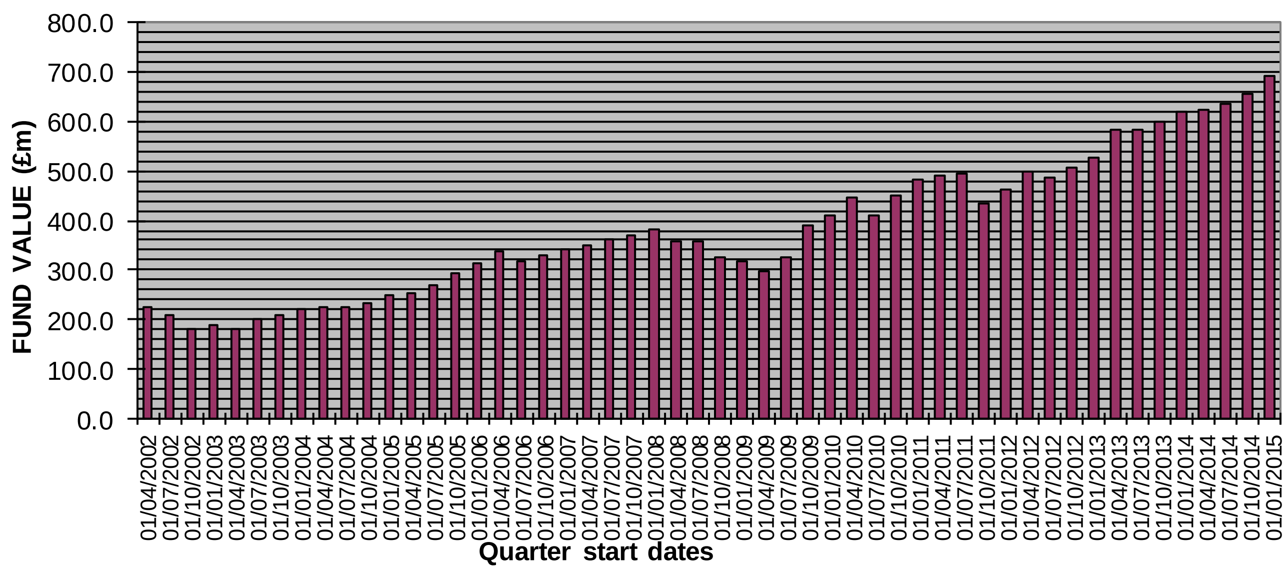
MOVEMENTS IN PENSION FUND MARKET VALUE SINCE 2002

Date	Baillie Gifford					Fidelity			Blackrock	MFS	Standard Life	CAAM	
	Balanced Mandate	DGF	Fixed Income	Global Equities	Total	Balanced Mandate	Fixed Income	Total	Global Equities	Global Equities	DGF	LDI Investment	GRAND TOTAL
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
31/03/2002	113.3				113.3	112.9		112.9					226.2
31/03/2003	90.2				90.2	90.1		90.1					180.3
31/03/2004	113.1				113.1	112.9		112.9					226.0
31/03/2005	128.5				128.5	126.6		126.6					255.1
31/03/2006	172.2				172.2	164.1		164.1					336.3
31/03/2007	156.0				156.0	150.1		150.1				43.5	349.6
31/03/2008	162.0				162.0	151.3		151.3				44.0	357.3
31/03/2009	154.6				154.6	143.5		143.5					298.1
31/03/2010	235.5				235.5	210.9		210.9					446.4
31/03/2011	262.7				262.7	227.0		227.0					489.7
31/03/2012	269.9				269.9	229.6		229.6					499.5
31/03/2013#	315.6	26.5			342.1	215.7		215.7			26.1		583.9
31/03/2014@	15.1	26.8	45.2	207.8	294.9		58.4	58.4	122.1	123.1	27.0		625.5
30/06/2014		43.0	46.1	208.9	298.0		59.7	59.7	126.5	125.5	27.3		637.0
30/09/2014		43.8	48.1	213.3	305.2		61.5	61.5	131.6	129.5	28.1		655.9
31/12/2014		44.0	50.2	227.7	321.9		64.9	64.9	139.3	139.2	28.4		693.7
31/01/2015		45.0	52.6	233.5	331.1		67.3	67.3	144.0	143.5	29.0		714.9

\# £50m Fidelity equities sold in Dec 2012 to fund Standard Life and Baillie Gifford DGF allocations.

@ Assets sold by Fidelity (£170m) and Baillie Gifford (£70m) in Dec 2013 to fund MFS and Blackrock global equities.

PENSION FUND - QUARTERLY VALUES SINCE 2002



Baillie Gifford Report for the quarter ended 31 December 2014

Quarterly portfolio information

Summary portfolio valuation and performance			
	30 Sept 2014	31 Dec 2014	3 month Performance to 31 Dec 2014
Global Alpha (gross)	£213,321,627	£227,724,878	6.6%
MSCI ACWI			*4.5%*
Diversified Growth (net)	£43,767,275	£44,039,768	0.6%
Base rate +3.5%			*1.0%*
Sterling Aggregate (gross)	£48,144,437	£50,152,287	4.17%
50% FTSE Actuaries UK Conventional Gilts All Stocks Index & 50% BoAML Sterling Non-Gilt Index			5.33%

Longer Term Performance

Performance to 31 December 2014 (%)

	Fund Gross	Fund Net	Benchmark
Since Inception* (Cumulative)	162.3	153.3	124.3
Since Inception* (p.a.)	6.6	6.4	5.5
Five Years (p.a.)	11.5	11.3	9.4
One Year	11.8	11.4	11.2
Quarter	6.7	6.6	4.5

*Inception date 31 December 1999
Global Alpha performance measurement began on 31 December 2013
Source: StatPro

Baillie Gifford was appointed in 1999 to manage a multi asset portfolio for the London Borough of Bromley. This portfolio was re-organised in December 2013 to the new mandate, Global Alpha, with funds being transferred to separate bond and Diversified Growth portfolios. The longer term performance of the Global Alpha portfolio therefore incorporates the longer term performance of the multi-asset portfolio.

Background

A violent plunge in the oil price was caused by OPEC's late-November meeting when the cartel of oil producing nations failed to cut production targets. This, and the flood of US shale, led to an imbalance of supply and demand and the oil price lurched sharply downward. Brent finished the year at $56, a drop of $39 on the level at the start of October. The negative ramifications are being felt most acutely in Russia, the economy of which remains precariously reliant upon its oleaginous exports. A leap in interest rates to 17% failed to shore up the crumbling ruble; these rates of interest were last seen in 1998, when the Russian government defaulted on its debt. On the positive side, the precipitous fall in the oil price is estimated to represent at least a 0.5% boost to global GDP in 2015. By comparison to the gyrations in the energy market, the stumbling recovery in Europe, another Japanese recession and robust job growth in the US seem mundane. The global index fell sharply early in the quarter, recovered and then stepped back before recovering once more as volatility, as measured by the VIX index, rose to levels last seen in late 2012. The global equity index (MSCI ACWI) rose by 4.5% in sterling terms over the quarter.

Global Alpha Portfolio

Japan is ripe for change and part of our research effort has focused on opportunities that reform may present. The consensus is one of scepticism towards Prime Minister Abe's reform policies. Following two research trips we are inclined to take a different view and we have an increasing belief in the reform agenda which we think will help both traditional Japanese companies and those that are prospering by rejecting the norms of Japanese orthodox corporate culture. As a result of this research, we added two new Japanese companies to your portfolio. CyberAgent is the leading digital advertising agency in Japan. It combines a strong core franchise and a culture that supports the development of new businesses including a blogging platform and social gaming. In addition, it has a venture capital unit with a portfolio of dynamic early stage technology companies in Japan and other parts of Asia. Insurance company MS&AD should benefit from reform in two ways. It has its own self-help plans – improving underwriting profits through a re-pricing of policies and increasing overseas earnings through organic growth. It can also benefit from reform by proxy through its ownership of Japanese equities within its insurance portfolio as traditional companies sharpen their focus on shareholder value. Elsewhere and maintaining this theme of 'change', we have purchased another reforming company in Fiat Chrysler Automobiles which has ambitious plans to grow through leading automotive brands such as Maserati, Jeep, Chrysler and Alfa Romeo. We also bought Monsanto, the global leader in seeds, plant biotechnology and crop protection, the future of which is less dependent on US corn than its past.

We sold three long-term holdings from your portfolio to fund these purchases. The shares of China Mobile have enjoyed a re-rating this year but we think the longer-term prospects are increasingly dull. We have owned Investor since the fund's inception in 2005. Whilst the guiding hand of the Wallenberg family is still firmly on the tiller of this Swedish holding company, the discount to net asset value has narrowed and we have become increasingly underwhelmed by some of its largest holdings. We also sold New York Community Bank, whose performance has been lacklustre in the past few years. We hoped it would regain market share in its core business of rent-regulated, multi-family housing units in metropolitan New York and that net interest margins would recover. However, neither scenario has played out as we would have hoped and the company's earnings power has not recovered substantially.

In 2014, Global Alpha's portfolio turnover has remained low and for the sixth year in a row it will be below the long-term average of 20%.

Outlook

In the early days of the quarter, when markets were once again under stress, we were continuing to find that the majority of the companies we own on your behalf were still reporting strong growth and many were seeing earnings upgrades just as share prices were falling sharply.

Equities are a high volatility asset class, and markets are not always logical so it is reasonable to conclude that, looking forward to 2015, there will be further periods when fundamentals and share prices become disconnected. Short-term or even inconsequential news flow will inevitably be extrapolated and exaggerated by Mr. Market. Guarding against this myopic short-termism, our job is to closely monitor the fundamentals of the businesses we own on your behalf, and keep a check on the progress they are making towards the goals we think they can achieve.

Shortly we will share with you our 2015 Research Agenda. We have used the preceding agendas successfully over the past three years to drive forward our efforts to unearth some exciting new growth ideas. Our optimism can usually be measured by how many new stocks are emerging for consideration, and there has been an uptick in this metric in recent months. The headlines will once again be filled with seemingly important macro-economic news, but we think that long-term corporate value lies in fundamentals. It is our adherence to this philosophy that gives us confidence that we can continue to deliver very worthwhile active equity returns.

EARLY RETIREMENTS

A summary of early retirements by employees in Bromley's Pension Fund in the current year and in previous years is shown in the table below. With regard to retirements on ill-health grounds, this allows a comparison to be made between their actual cost and the cost assumed by the actuary in the triennial valuation. If the actual cost of ill-health retirements significantly exceeds the assumed cost, the actuary will be required to consider whether the employer's contribution rate should be reviewed in advance of the next full valuation. In the latest valuation of the Fund (as at 31st March 2013), the actuary assumed a figure of £1m p.a from 2014/15, a significant increase over the estimate of £82k p.a. in the 2010 valuation. In 2013/14, there were six ill-health retirements with a long-term cost of £330k and, in the first three quarters of 2014/15, there were three ill-health retirements with a long-term cost of £257k. Provision has been made in the Council's budget for these costs and contributions have been or will be made to reimburse the Pension Fund, as result of which the level of costs will have no impact on the employer contribution rate.

The actuary does not make any allowance for other (non-ill-health) early retirements, however, because it is the Council's policy to fund these in full by additional voluntary contributions. In 2013/14, there were 26 other retirements with a total long-term cost of £548k and, in the first three quarters of 2014/15, there were 16 non ill-health retirements with a long-term cost of £196k. Provision has been made in the Council's budget for severance costs arising from LBB staff redundancies and contributions have been or will be made to the Pension Fund in both years to offset these costs. The costs of non-LBB early retirements have been recovered from the relevant employers.

Long-term cost of early retirements	**Ill-Health**		**Other**	
	No	£000	No	£000
Qtr 3 – Dec 14 - LBB	-	-	3	64
- Other	-	-	-	-
- Total	-	-	3	64
Total 2014/15 – LBB	2	203	13	154
- other	1	54	3	42
- Total	3	257	16	196
Actuary's assumption - 2013 to 2016		1,000 p.a.		N/a
- 2010 to 2013		82 p.a.		N/a
Previous years – 2013/14	6	330	26	548
– 2012/13	2	235	45	980
– 2011/12	6	500	58	1,194
- 2010/11	1	94	23	386

PENSION FUND REVENUE ACCOUNT AND MEMBERSHIP

	Final Outturn 2013/14 £'000's	Estimate 2014/15 £'000's	Actual to 31/12/14 £'000's
INCOME			
Employee Contributions	5,580	5,600	4,450
Employer Contributions	23,967	23,000	17,540
Transfer Values Receivable	5,074	3,000	2,360
Investment Income	10,883	7,000	5,130
Total Income	45,504	38,600	29,480
EXPENDITURE			
Pensions	23,409	24,300	18,290
Lump Sums	5,884	6,000	3,640
Transfer Values Paid	1,559	3,000	3,170
Administration	2,413	2,500	1,870
Refund of Contributions	13	-	60
Total Expenditure	33,278	35,800	27,030
Surplus/Deficit (-)	12,226	2,800	2,450

MEMBERSHIP	**31/03/2014**	**31/12/2014**
Employees	5,254	5,637
Pensioners	4,862	4,937
Deferred Pensioners	4,819	5,007
	14,935	15,581

AllenbridgeEpic
investment advisers

APPENDIX 5

REPORT PREPARED FOR

London Borough of Bromley Pension Fund

Fund performance to 31st December 2015

6 February 2015

Alick Stevenson
AllenbridgeEpic Investment Advisers Limited (AllenbridgeEpic)

alick.stevenson@allenbridgeepic.com
www.allenbridgeepic.com

This quarterly report by your adviser, Alick Stevenson of AllenbridgeEpic Investment Advisers (AllenbridgeEpic), provides a summary of performance and an analysis of the investments of the London Borough of Bromley Pension Fund for the three months ending 31 December 2014.

Market Summary 4th Quarter 2014

"It's tough to make predictions, especially about the future."
Yogi Berra

2014 was a year of market volatility, and a year in which the UK and US central banks halted their quantitative easing programmes, in which the Japanese central bank launched its own programme and a year in which the European central bank did nothing apart from talk.

It was a year in which various conflicts threatened to derail the global recovery, and a year in which the oil producers (Middle Eastern States) refused to reduce their output in the face of significantly weaker demand causing the oil price to fall to levels not seen for 5 years, and the major oil companies to rapidly scale back their capital expenditure and exploration programmes coupled with announcements regarding smaller workforces.

It was a year that saw President Obama lose control of both the Senate and the House of Representatives creating what is known as a "lame duck" presidency for the remaining period of his second term and latterly the year in which the opening salvos were fired in the run up to the UK General Election in May 2015.

2014 saw growth in the USA and the UK offset by no growth in Europe, patchy growth in Japan and the Far East and extreme volatility in emerging markets.

Whilst inflation itself was not a problem for the markets, the lack of consumer spending, despite low interest rates and significantly lower pump prices for fuel, raised the spectre of deflation, especially in Europe where unemployment is reaching crisis levels and Greece once again threatens the stability of the Euro which fell to its lowest levels against the US dollar for more than four years.

Investment houses also suffered: PIMCO saw Bill Gross walk out to join Janus Capital with a subsequent halving in assets under management of the PIMCO flagship bond fund. Baring Asset Management suffered a similar walk out of three top investment managers and a subsequent drop of over 60% in the value of their DAA and MAF diversified growth funds and Invesco lost Neil Woodford to his new investment company taking several billion pounds of assets with him. Whilst Aberdeen Asset Management, struggling to absorb SWIP, saw major outflows from its emerging market funds coupled with nondescript investment performance in its equity and bond portfolios.

The only "winners" appeared to be the investment houses running passive portfolios who reported significant inflows from investors seeking a move away from active management and higher fee structures and other houses offering DGF products which benefitted from Baring woes.

Looking forward into 2015, the crystal ball is murky. Suffice it to say that we may well see the first interest rate rises for several years, continued volatility in the stock and bond markets as commentators analyse the central bank pronouncements all in all, it's likely to be a bumpy ride, as Mae West once famously said.

I'm ending this Market Summary with a clip from my report for the **quarter ended 31 December 2013,** in which I wrote

"Key issues facing the markets as we move into 2014 include:

- *Central banks' ability to manage "tapering" without derailing the nascent recovery, causing inflation to surge, and at the same time keeping the markets "happy"?*
- *Will global growth continue to improve slowly and broadly?*
- *No significant fiscal problems in the Eurozone?*
- *No market perceived "bubbles" in asset prices leading to increased volatility and potential market declines."?*

Inflation continues to fall on the back of lower oil prices which impact positively on consumer prices and so on. However, it's the fear of deflation leading to stagnation and the "Japanese disease" that worries markets.

"Déjà vu all over again" ***Yogi Berra***

Executive Summary

- **The fund had a good quarter, rising in value to £693.7m as at 31 December 2014 from £655.9m at 30 September 2014. The corresponding figure for 31 December 2013 was £618.8m.**

- **Investment performance was good with the fund delivering a strong 5.6% net of fees (benchmark 4.3%) return for the quarter, 12.1% (10.9%) for the rolling twelve months and 14.6%pa (12.3%pa) over the rolling three year period. These figures compare positively to the current actuarial assumption of 5.6%pa.**

- **Baillie Gifford reported the resignation of one of their fund managers on the Multi asset team. See Page 6 for a more detailed note.**

- **BlackRock reported some changes in their client relationship management. See Page 7 for a more detailed note.**

Fund Matters

The Third Phase of the investment reorganisation (that of reorganising the fixed income assets) continues. The latest update is provided in a separate report on this agenda.

Fund Value as at 31 December 2014

As far as the strategic or long term asset allocations are concerned, the fund remains slightly overweight equities and DGF assets and remains underweight fixed interest. These over and underweight positions will be closely monitored and may be adjusted following completion of the Phase 3 Fixed Income restructuring.

It is worth noting, although not for any immediate action, that Baillie Gifford manage approximately 46% of the total fund assets as at 31 December 2014. This compares with 58.5% as at 31 December 2012 and 45% as at 31 December 2013.

Manager		Asset	Value	Actual		Value	Actual		Strategic
Name		Class	31-Dec-14 £m	% of Fund		30-Sep-14 £m	% of Fund		Asset Allocation %
Baillie Gifford Standard Life		DGF DGF	44.0 28.4			43.8 28.1	6.7 4.3		
Sub total DGF			72.4	10.4		71.9	11.0		10.0
Baillie Gifford BlackRock MFS		Global E Global E Global E	227.7 139.3 139.2			213.3 131.6 129.5	32.5 20.1 19.7		
Baillie Gifford Fidelity		Fixed Int Fixed Int	50.2 64.9			48.1 61.5	7.3 9.4		
Sub total GE			506.2	73.0		474.4	72.3		70.0
Sub total FI			115.1	16.6		109.6	16.7		20.0
BG Fidelity									
Sub total cash			0.0			0.0	0.0		0
Fund Totals			693.7	100.0		655.9	100.0		100.0

Source: manager reports and WM investment services

Overall Fund investment performance for the quarter under review is shown on the next page.
A more detailed manager specific analysis is provided within each Investment manager report beginning on Page 6.

Summary

Fund Return		5.6
Benchmark Return		4.3
Relative Performance		1.3
	attributable to:	
	Asset Allocation	-0.1
	Stock Selection	1.4

Asset Allocation

	Total Equity	UK Bonds	Multi Asset	Cash	Total Fund
Fund Start	71.5	16.7	11.0	0.8	100.0
Fund End	72.3	16.6	10.4	0.7	100.0
BM Start	70.0	20.0	10.0		100.0
BM End	70.1	20.2	9.7		100.0
Impact	-	-	-	-	-0.1
Diff	1.5	-3.3	1.0	0.8	0.0
	2.1	-3.6	0.7	0.7	0.0

Stock Selection

	Total Equity	UK Bonds	Multi Asset	Cash	Total Fund
Fund	6.7	4.8	0.8	0.4	5.6
Benchmark	4.5	5.1	1.2		4.3
Impact	1.5	-	-		1.4
	2.1	-0.3	-0.3		1.3

Source: WM investment services

It is clear from the above charts that asset allocation has had a negligible negative impact on overall investment performance whereas stock selection was extremely robust, reflecting positively on the active manager structure.

Manager Changes

There is one change at Baillie Gifford which was highlighted in the Executive Summary and is explained in more detail in the Baillie Gifford review below.

BlackRock has also made some changes which are further explained in the BlackRock review on Page 7. Neither of these changes should affect the way in which the portfolio is managed.

No other changes that would affect the running of the various portfolios have been notified by the investment managers.

Fund Governance and Voting

Voting and governance matters are covered in some detail within the various Investment Manager reports provided to the members under separate cover. Both BlackRock and MFS will be attending the PISC on 24 February 2015 and will respond to any questions members may have on voting and governance policies.

Investment Manager Reviews

GLOBAL EQUITY PORTFOLIOS

Baillie Gifford Global Alpha (segregated)

This portfolio was funded as at 20 December 2013.

Performance objective: to outperform the MSCI ("ACWI") All Country World Index by 2-3% pa (before fees) over rolling five year periods.

Fund positioning was little different from the previous quarter with just minor changes; previous quarter numbers in brackets. At the end of December 2014, the global equity fund was invested across 25 (24) countries and held 97 (94) different investments. These investments were spread over 8 (9) sectors and encompassed 40 (43) differing industries, thus providing a broadly diversified set of assets. It is worth noting that the active money within this portfolio is continuing to run at 92% (92%). This implies that the fund is not holding benchmark or index weightings relating to stocks making up the index and reflects the active stock picking philosophy of the manager.

For the quarter, the manager achieved a net return of 6.6% (benchmark 4.5%). Since inception, the manager has achieved a positive return of 6.4% pa (gross of fees, 6.2%pa net) against the benchmark of 5.5% pa.

In terms of regional allocations Baillie Gifford remains significantly underweight North America (46.8% v 55.9%) and underweight Developed Asia Pacific (10.5% v 11.2%) but is running an overweight to Emerging Markets (+13.5% against an index weighting of 10.3%) and a small overweight in the UK.

The "active money" style (stock picking) is clearly demonstrated with the top ten holdings accounting for nearly 25% (24%) of the total portfolio. Prudential at 3.4%, Royal Caribbean Cruises at 4.1% and Naspers at 3.4%, retain the top three names whilst Anthem Inc, Amazon and Google take the bottom three positions with 1.9%, 1.8% and 1.8% respectively.

Mike Brooks, was one of the original team at BG who developed the multi asset product, and who pitched to the PISC back in 2012, has decided to leave BG for a position with another firm. In a conversation with Ken Barker and Geraldine Deighan, Ken explained that leaves the team with three fund managers, three analysts and two investment assistants. They will be monitoring the situation over the next few months and do not rule out additional hires. Whilst a loss to Baillie Gifford, this is not a matter for major concern. We will, of course, continue to monitor the fund on a regular basis and will make the members aware of any future concerns.

BlackRock Ascent Life Enhanced Global Equity Fund (pooled)

This portfolio was funded as at 20 December 2013.

Performance objective: to outperform the MSCI ACWI by 1-2% per annum whilst managing risk relative to the benchmark.

The manager can invest across the whole of the ACW Index and, as a result, held 846 stocks (716) at the end of the quarter and outperformed its benchmark by 1.3% (5.8% v benchmark 4.5%) in the quarter. Since inception the fund has performed strongly and has achieved a return of 15.5% against a benchmark of 12.9%.

In terms of country risk, the manager is slightly overweight Japan and Germany and underweight North America (USA and Canada), the UK and "Other Countries". Sectorally, the fund has remained overweight Info Tech, Telecoms and Utilities and continues with its underweight positions in Consumer Discretionary and Consumer Staples, Financials and Materials.

Top ten stocks are little changed from last quarter with Verizon (1.6%) and Pfizer (1.6%) and Union Pacific Corp (1.4%) talking the top three positions. However, it should be mentioned that last quarter Apple held the top spot, but BlackRock took the view that its valuation was becoming a bit "stretched" and sold the holding down from approx. 2.8% to just 0.95% of the fund.

The importance of Local Authority Pension Funds to Blackrock, across a wide variety of asset classes and potential significant change, has led to the recent formation of a specialist LGPS team which will focus on delivering the very special needs that an LGPS has. Responsibility for managing the Bromley relationship has been taken on by Simon Betteley who will continue to be supported by Ahsan Abdullah as our day to day contact.

BlackRock executives will be in attendance at the PISC meeting on 24 February.

MFS Global Equity Fund (segregated)

This portfolio was funded as at 18 December 2013.

Performance objective: to outperform the MSCI world index (net dividends reinvested) over full market cycles.

MFS currently invests in 15 (15) countries and has 109 (111) holdings. This contrasts with the benchmark of 1,636 holdings spread across 24 countries. In the December quarter, the fund performed well (7.3% v benchmark 4.4%). Since inception the fund has returned 15.4% gross (14.84% net) against the benchmark of 12.1% gross (11.54% net).

Looking through the country and sector weights shows that the fund is currently underweight North America (52.4% v 60.6%) and Asia Pacific ex Japan (1.1% v 4.8%), and has maintained the overweight positions in Europe ex UK (+2.5%), UK (+2.1%) and Japan (+4.1%). The fund is also running a small +1.1% overweight in emerging markets.

Sectorally, the fund has again maintained its significant overweight position in Consumer Staples (+19.3% v 9.9%), with small overweights in Industrials (+3.7%) and Telecommunication Services (+2.0%). These over weights are being "funded" by underweight positions in Information Technology (-2.8%), Consumer Discretionary (-3.6%), Utilities (-3.4%) , Energy (-3.2%) and Materials (-3.2%).

In terms of holdings, KDDI Corporation with 2.6% of the portfolio and Johnson & Johnson at 2.3% are the two largest. Novartis and Pfizer at 1.8% and 1.8% respectively are in ninth and tenth positions.

MFS executives will be in attendance at the PISC meeting on 24 February 2015.

Global Equity Crossholdings

Of the top ten holdings by manager only two stocks **are held in size** by more than one manager. In aggregate it must be said that they represent just 0.13% of the total fund of £693.7m

Pfizer, 1.7% by MFS and 1.6% by BlackRock (value of total holdings £4.6m)
Johnson & Johnson 2.3% by MFS and 1.1% by Blackrock (value of total holdings £4.7m)

DIVERSIFIED GROWTH FUNDS

Overall, Baillie Gifford has maintained its much lower allocation to global equities, but has retained a higher allocation to both high yield and emerging market bonds. In addition BG continues to favour structured finance, property and insurance linked assets.

In contrast, Standard Life holds just over 47% of its assets in derivative based investments backed by cash, favouring its relative value and directional investment strategies.

Baillie Gifford Diversified Growth Fund

Performance objective: to outperform UK base rate by at least 3.5% pa (net of fees) over rolling five year periods and with an annualised volatility of less than 10%.

The fund has performed well since its inception in December 2012 generating a net return of 5.7% against the benchmark of 4.0%. For the 12 month period it has returned 5.3% against the benchmark of 4.0%. For the quarter the fund had a return of 0.6% versus the benchmark of 1.0%.

The performance in the quarter was primarily due to positions in absolute return, listed equities and property, whilst active currency positions were a negative contributor this quarter. Most other asset classes were broadly flat over the quarter.

There were few major changes to the overall asset allocations over the quarter, the exceptions being increased investment in listed equities to 21.85 (17.7%) and high yield bonds to 11.7% (9.3%) funded from cash and minor adjustments to cash and investment grade bonds.

One of the primary directives for the fund, and one closely followed, is to keep the volatility within target. At the end of the quarter the current figure was similar to that at the end of the previous quarter 4.7% (4.7%) well within the upper ceiling of +10%.

Standard Life Global Absolute Return Fund

Performance objective: to achieve +5% per year (gross) over 6 month LIBOR over rolling three year periods with expected volatility in the range of 4% to 8%

GARS continues to deliver strong results in all periods since inception.

For the quarter the manager delivered 1.2% net of fees against the benchmark of 1.4%, and since inception a gross return of 6.4% versus a benchmark of 5.6%.

Positive contributions from directional currency investments, global equities and global REITs investments were partially offset by losses on relative value investments. It should be noted that GARS no longer holds an investment in REITs as the fund managers sold their holdings as the targeted return was achieved. Despite various market "shocks", volatility within GARS was held at just 3.9% for the second consecutive quarter.

In terms of construction, the fund is running some 30 different strategies with approximately 42% (40%) invested in directional, 33% (31%) in market return assets, 23% (26%) in relative value and approximately 2% (3%) in security selection.

As noted above, asset allocations at the end of this quarter were almost exactly the same as those at the end of the third and second quarters. The profitable liquidation of the REIT investment was partly taken up by a small increase in emerging market bonds, with the balance held in cash and cash equivalents.

The chart below highlights the asset allocation differences between Baillie Gifford and Standard Life in sourcing investment returns

	Baillie Gifford	Baillie Gifford	Standard Life	Standard Life	Total DGF	Total DGF
	%	£m	%	£m	£m	%
Value at 31 Dec 2014		44.0		28.4	72.5	
Asset Class						
Global equities	21.8	9.6	33.4	9.5	19.1	26.3
Private equity	2.0	0.9			0.9	1.2
Property	2.1	0.9			0.9	1.3
Global REITS				0.0	0.0	0.0
Commodities	5.4	2.4			2.4	3.3
Bonds						
High yield	11.7	5.2	4.5	1.3	6.4	8.9
Investment grade	6.3	2.8	5.8	1.6	4.4	6.1
Emerging markets	13.0	5.7	8.8	2.5	8.2	11.3
UK corp bonds						
EU corp bonds						
Government		0.0			0.0	0.0
Global index linked						
Structured finance	13.7	6.0			6.0	8.3
Infrastructure	4.4	1.9			1.9	2.7
Absolute return	8.1	3.6			3.6	4.9
Insurance Linked	5.3	2.3			2.3	3.2
Special opportunities	0.6	0.3		0.0	0.3	0.4
Active currency	-0.9	-0.4			-0.4	-0.5
Cash	6.6	2.9			2.9	4.0
Cash and derivatives			47.6	13.5	13.5	18.7
Total	100.1	**44.1**	100.1	**28.4**	**72.5**	100.0

Numbers may not add due to roundings

Source: Baillie Gifford and Standard Life

FIXED INCOME PORTFOLIOS

Baillie Gifford Aggregate Plus Portfolio

Performance objective: to outperform by 1.5% pa (gross of fees) a benchmark comprising 50% FTSE UL conventional All Stocks index and 50% Bank of America Merrill Lynch Sterling Non Gilt index over rolling three year periods.

The fund had a return of 4.1% (net of fees) in the quarter against the benchmark of 5.3% with the majority of that underperformance coming from adverse currency movements. Since inception, the fund has returned 12.5% against a benchmark of 11.9%.

Portfolio duration is slightly longer than the benchmark at 9.15 years versus 8.92 years and was a small contributor to performance.

From a credit rating perspective, the fund is slightly overweight benchmark with AAA rated bonds, underweight AA (-7.1% to the benchmark) and overweight BBB (at +3.8% to the benchmark).

High yield, or below investment grade, has an overweight of 32.8% to the index and is comprised largely of bonds which have lost their “BBB” rating, but in the opinion of the manager, have the ability to regain that rating.

In terms of active money, ie. those positions larger than the benchmark allocation, the manager holds 2.0% of the fund in EDF, 6% 2114 and 1.6% in DP World 2037 and Network Rail and 1.5% in each of Phoenix Life 2021 Perpetual and Friends provident 2022.

Fidelity Global Aggregate Fixed Income Portfolio

Performance objective: to outperform by 0.75% pa (gross of fees) a benchmark comprising 100% of (IBoxx Composite (50% Gilts and 50% £ Non Gilts) over rolling three year periods.

The fund performed in line with the benchmark during the quarter with a return of 5.4%. Over the last three years the fund is ahead of the benchmark by 2.7% pa (15.1% pa v 12.4%pa) and since inception (30 April 1998) has outperformed the benchmark by 0.8% pa.

In terms of credit ratings, the fund has nearly 70% invested in AAA, AA and A rated bonds, albeit underweight the index, especially in AA bonds, and has 19.6% invested in BBB rated bonds. The manager has maintained a small position 2.8% (4.0%) in high yield bonds and holds the remaining 6% in a mix of cash and unrated investments.

There has been almost no change at all during the quarter to the sectoral allocations with US treasury assets accounting for approximately just over 43% (40%) of the portfolio. Overweight positions in the Financial Services, Communications and Insurance sectors are offset by underweights in Supranationals and Sovereign Assets and Utilities.

The portfolio is in line with the duration of the benchmark 9.3 years (versus 9.2 years) and has a running yield of just 2.9%.

Alick Stevenson
Senior Adviser
AllenbridgeEpic Investment Adviser

Report No.
FSD15016

London Borough of Bromley

PART 1 - PUBLIC

Decision Maker:	**Pensions Investment Sub-Committee**		
Date:	**24th February 2015**		
Decision Type:	Non-Urgent	Non-Executive	Non-Key
Title:	**REVISED INVESTMENT STRATEGY - PHASE 3**		
Contact Officer:	Martin Reeves, Principal Accountant (Technical & Control) Tel: 020 8313 4291 E-mail: martin.reeves@bromley.gov.uk		
Chief Officer:	Director of Finance		
Ward:	All		

---

1. Reason for report

This report provides further information on “alternative fixed income (inflation proofing / illiquid)” assets as part of the 20% “protection” allocation under phase 3 of the investment strategy agreed in 2012. The Sub-Committee is asked to consider the attached report from the Fund’s advisers, AllenbridgeEpic, which recommends a gradual move in Fidelity’s fixed income holding from the existing UK Aggregate Bond Fund to the Fixed Income Diversified Alpha (FIDA) Fund.

RECOMMENDATIONS

The Sub-Committee is asked to:

2.1 Note the report and to:

a) Agree to invest an initial £5m in Fidelity’s FIDA Fund, to be transferred from Fidelity’s existing UK Aggregate Bond Fund, with further quarterly transfers to be made dependent on investment performance and the overall size of the fund; and

b) Agree that Baillie Gifford continue to manage the remainder of the fixed income portfolio under their existing Sterling Aggregate Bond Fund.

Corporate Policy

1. Policy Status: Existing policy. The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2013, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

2. BBB Priority: Excellent Council.

Financial

1. Cost of proposal: No cost

2. Ongoing costs: N/A.

3. Budget head/performance centre: Pension Fund

4. Total current budget for this head: £35.8m expenditure in 2014/15 (pensions, lump sums, admin, etc); £38.6m income (contributions, investment income, etc); £693.7m total fund value at 31st December 2014)

5. Source of funding: Contributions to Pension Fund

Staff

1. Number of staff (current and additional): 0.4 fte (current)

2. If from existing staff resources, number of staff hours: c14 hours per week

---

Legal

1. Legal Requirement: Statutory requirement. Local Government Pension Scheme (LGPS) Regulations 2013

2. Call-in: Call-in is not applicable.

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 5,637 current employees; 4,937 pensioners; 5,007 deferred pensioners (as at 31st December 2014)

Ward Councillor Views

1. Have Ward Councillors been asked for comments? No.

2. Summary of Ward Councillors comments: N/A

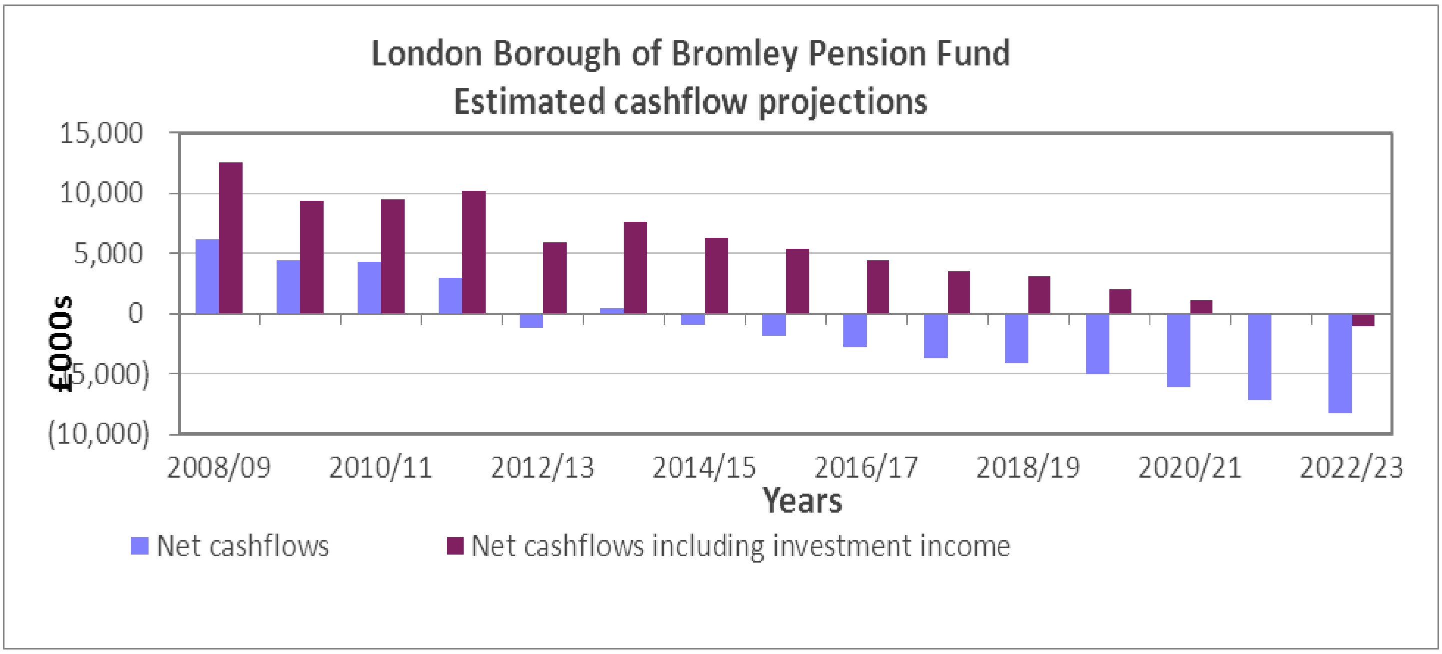
3. COMMENTARY

3.1 In February 2012, the Sub-Committee agreed a future strategy for the Fund, comprising a 10% allocation to Diversified Growth, a 70% allocation to global equities and a 20% allocation to fixed income (corporate bonds/gilts). It was agreed that the revised strategy would be implemented in three separate phases and, following a "beauty parade" in November 2012, Phase 1 was completed on 6th December 2012 with the award of two Diversified Growth Fund mandates of £25m to Baillie Gifford and Standard Life. A further "beauty parade" at the special meeting in October 2013 resulted in the completion of Phase 2 with the award of three global equities mandates to Baillie Gifford (£200m), Blackrock (£120m) and MFS (£120m).

3.2 AllenbridgeEpic have previously been appointed to provide specialist procurement advice for the implementation of the revised strategy and have managed the processes for Phase 1 and Phase 2. At the meeting in November 2013, Members considered an initial update from AllenbridgeEpic on Phase 3 of the revised investment strategy (fixed income). It was agreed that the Fund should enter into arrangements with one or more managers for global fixed income pooled funds (at its meeting in February 2012, the Sub-Committee had originally agreed that two managers be appointed). It was also agreed that the procurement process for Phase 3 be run on the basis that investment would be made in global fixed income pooled funds. Pooled funds fall outside the EU procurement rules because they are considered to be direct investment decisions (there is an exemption for financial instruments). Accordingly, although we would still have to tender for the mandate(s), we would not have to follow the OJEU route, which would shorten the tender process. At that stage, the timetable indicated that Phase 3 should be completed (funded) by 31st March 2014.

3.3 In accordance with the investment strategy agreed in 2012, 20% of the Bromley Fund would be allocated to fixed income, which, based on the current Fund value, would be around £140m. At the November 2013 meeting, however, a Member questioned whether 20% was too high given higher returns he felt could be achieved from other investments. Fixed income assets provide cash for the Fund, but are, over time, likely to generate a return of "only" 3% to 6%, which is considerably less than we would expect from, say, global equities. Members asked for the Scheme Actuary to prepare a cash flow projection for the Fund in order to better identify the length of time potentially remaining before the Fund moves to "cash neutral" and then to "cash negative". The cashflow forecast would help inform subsequent investment debates and decisions by the Sub-Committee in terms of investing the assets of the fund in income generating assets (fixed income characteristics), rather than growth seeking "risk" assets (equities).

3.4 The actuary prepared a cashflow projection and this was attached as an appendix to a further update report from AllenbridgeEpic that was considered at the Sub-Committee meeting in February 2014. The actuary advised that, based on the numbers in the projections, the Fund was likely to move into a net cashflow negative position (including investment income receipts) in around 2020/21. The Fund is currently cash positive once income from equities being re-invested is taken into account, but, excluding investment returns, became cash-negative in 2012/13 and the actuary expects this position to generally get worse. Put simply, it is possible to say that net dealings with members put the Fund in a cashflow negative position and investment income might be needed each year going forwards from now on to pay benefits due. The actuary's cashflow projection is shown below.



3.5 At that February meeting, Members agreed to defer a decision on the final allocation to fixed income and requested a report to the next meeting of the Sub-Committee on alternative "protection type" assets as part of the fixed income allocation. The next meeting, originally scheduled in May, was cancelled because of the local elections and the matter was considered again in August 2014, when the Sub-Committee agreed that "a manager search be carried out seeking to appoint one or more managers to invest a total of up to 10% of the fund (c. £60m based on the current fund value) over the longer term in "alternative fixed interest (inflation proofing / illiquid)" assets; and that "the remaining balance of the 20% allocation for fixed income be managed by one (or both) of the existing fixed income managers (Baillie Gifford and Fidelity) on a global basis with an absolute return benchmark (as set out in the Statement of Investment Principles 2014)."

3.6 At the August meeting, there was some discussion around the appropriateness of investing 50% of the 20% "protection" allocation (c. £60m at that time) in fixed income and it was agreed that AllenbridgeEpic should research further into assets matching the criteria contained in the August report. They reported back to the Sub-Committee in December 2014 and the Sub-Committee agreed that, in view of Member concerns over the illiquidity of potential funds highlighted by AllenBridgeEpic, existing conventional fixed income assets be retained. AllenBridgeEpic were asked to continue to search for options at an appropriate level of risk, reporting back to this meeting. An update is attached as Appendix 1 and this recommends that the Baillie Gifford fixed income mandate continues unchanged, while, with regard to Fidelity, they recommend that an initial £5m be invested in Fidelity's FIDA Fund, to be transferred from Fidelity's existing UK Aggregate Bond Fund, with further quarterly transfers to be made dependent on investment performance and the overall size of the fund.

4. POLICY IMPLICATIONS

4.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2013, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

5.1 None at this stage.

Non-Applicable Sections:	Legal and Personnel Implications
Background Documents: (Access via Contact Officer)	LGPS (Administration) Regulations 2008 (as amended) and LGPS Regulations 2013. LGPS (Management & Investment of Funds) Regulations 2009.

This page is left intentionally blank

REPORT PREPARED FOR

London Borough of Bromley Pension Fund

Revised Investment Strategy – Phase 3 (Fixed Income)

10 February 2015

Alick Stevenson
AllenbridgeEpic Investment Advisers Limited (AllenbridgeEpic)

alick.stevenson@allenbridgeepic.com
www.allenbridgeepic.com

The process of reorganising the investments of the fund began in 2011 and was approved in 2012. The process was separated and managed in three phases,

Diversified Growth Funds	10%
Global equity portfolio	70% (80%)
Fixed income portfolio	20% (20%)

In addition, the appointed consultant (AllenbridgeEpic Investment Advisers), was instructed to consider and moderate the implications of these proposed changes on the governance budget in terms of both staffing levels and costs. It was noted that, whilst Baillie Gifford had performed well over many years and continued to deliver good investment returns in both equity and fixed income investments, Fidelity had slipped behind their benchmark with their equity returns although they continued to deliver strong results on fixed income.

The first phase was the creation of a Diversified Growth Fund portfolio which was concluded successfully in December 2012 with the appointment of Baillie Gifford and Standard Life. Funding for these two mandates came from a reduction in the equity assets managed by Fidelity.

The second and largest phase was to reorganise the regionalised equity portion of the fund into three separate global equity investment mandates enabling the fund to benefit from manager investment styles across a range of markets. This phase was concluded in December 2013 with the appointment of Baillie Gifford, BlackRock and MFS investment Management. Funding for these new mandates came from the remaining Fidelity equity assets, and a reduction in the equity assets held by Baillie Gifford.

At the end of the second phase, the fund had completed 80% of its reorganisation and had increased the number of investment managers from two to five, and the number of separate mandates from four (two each at Fidelity and Baillie Gifford) to seven.

Two DGF mandates
Three global equity mandates
Two fixed income mandates

Phase 3 Fixed Income

Whilst this final phase was originally looking to invest in global bond funds, the manager responses to an initial search in 2013/14 found very few managers with global reach and some that focussed on one sub asset class such as “global emerging market” or “global high yield”, yet described themselves as “global fixed income”. It was agreed in the first quarter of 2014 that the brief should be widened to include fixed income assets which had an “illiquidity premium” such as capital release bonds, infrastructure/renewable energy investments and social housing. At the May 2014 meeting of the PISC, it was agreed that, whilst an illiquidity premium had its attractions, further review was needed.

PISC 2 December 2014

At the meeting on 2 December 2014, members considered propositions for investment in illiquid assets and felt that the Committee needed more information before making any firm commitment in either asset class or amount.

It was agreed, however, that AllenbridgeEpic should consider alternative ways in which to improve investment returns whilst maintaining liquidity and transparency and present them at the next meeting of the PISC to be held on 24 February 2015.

Current fixed income Structure

L B Bromley Pension Fund is currently holding approx. £115.1m or approx. 17% of the total fund in fixed income assets (31 December 2014), split as follows:

Baillie Gifford
The original portfolio (comprising regional equities and fixed income) had an inception date of 30 November 1999. The reorganisation of the equity portfolio into a separate global equity mandate was completed on *31 December 2013* and the fixed income mandate changes were completed on *15 April 2014*
Fixed income value £50.2m as at 31 December 2014
The fixed income target is to outperform (before fees) a composite benchmark comprising 50% FTSE Actuaries UK Conventional Gilts All Stocks index, and 50% Bank of America Merrill Lynch Non-Gilt Index over rolling three year periods

Fidelity
Original inception (regional equities and fixed income) 30 April 1998
Value of fixed income fund £64.9m at 31 December 2014
The target is to achieve 0.75%pa over the iBoxx Composite Index (50% Gilts and 50% Non- Gilts) over rolling three year periods

Overall Fund

Based on current values and targets, the fixed income portfolio is set an aggregated return target of 1.0%pa (0.97% pa at current value split) over rolling three years (gross of fees).
As previously noted, investment in illiquid assets, infrastructure, social housing, property, long lease contracts, capital release bonds, etc, should provide an enhanced source of return because of the "illiquidity factor", but would have very limited market liquidity pending repayment at maturity. It is this lack of liquidity which concerns the members. My understanding of the discussions at the 2 December 2014 meeting, is that the Sub-Committee would rather be invested in liquid fixed income assets, in a more broadly based fund than is currently in place and which carries a higher out-performance target. We, (AllenbridgeEpic), have again looked at the market and considered various funds which purport to operate in the unconstrained global fixed income space and have found that very little change has taken place since we last looked in depth with several products invested in just one fixed income class or a mix of corporate and high yield, both of which are vulnerable to shifts in interest rates and economic change.

However, in discussion with Paul Harris (Fidelity), he mentioned a Fidelity product (Fidelity Fixed Income Diversified Alpha) ("FIDA") which might be of interest. As a result, I met with Peter Khan, (Portfolio Manager FIDA, who also manages the Fidelity High Yield and Fidelity Global Income Fund) and Rob Marsden (Investment Director) on 14 January 2015, who walked me through a 90 minute presentation on FIDA.

In some respects, FIDA is similar to the Standard Life "GARS" Fund in which the L B Bromley Pension Fund has been successfully invested since December 2013, albeit GARS invests across a significant number of different asset classes and products rather than just one broad asset class.

FIDA takes an active absolute return approach to fixed income investing with a target return of 1.5% to 3.0% over cash (one month EURIBOR), gross of fees which would be in the 40/50 bps range. FIDA is broadly market neutral and seeks to generate alpha (at least 10bps) from each high conviction idea from eleven different diverse sources, whilst maintaining volatility between 2 and 5.0% per annum and operates a very conservative and focussed buy/sell risk measurement process.

Its three key themes are:

- Attractive risk adjusted returns
- Strong capital preservation
- Low volatility

This volatility target is slightly below that of Baillie Gifford (4.7%) and GARS (4.3%) as at year end. FIDA is currently relatively small (around 50m), but has additional current investor interest which Fidelity hopes will be converted into additional aum. This is one of the reasons I recommend a "drip feed" methodology. It is true to say that an investment of this size is unlikely to have a visible impact on the overall fund return, however, it provides a broad based allocation of funds at a time when single asset class funds are struggling to find positive returns over inflation.

The L B Bromley Pension Fund has two fixed income managers who have delivered positive results for many years, Baillie Gifford has only recently reorganised its fixed interest portfolio, whilst the Fidelity portfolio has been in situ since April 1998. It is possible that a further search could identify another manager(s) with a good track record although completion and funding would probably take at least three months (under a non OJEU process), would incur transition costs and would add an additional manager to the existing list, with additional governance implications.

We consider this Fidelity product to be one of the better offerings for several reasons:

- Fidelity is well known to the Pension Fund
- Consistent delivery of positive returns to benchmark with the existing mandate
- Fidelity is a significant investment manager in the Local Authority market
- Minimal new documentation needs
- No need for an external manager search
- Lower all round costs to the fund and a very speedy implementation process

Because FIDA is within the Fidelity Investment Management Group, the Pension Fund could simply appoint Fidelity to run this new fund alongside its existing UK Aggregate Fund and drip feed funds across. There is no need for the Fund to effect an open market search for a new product and as such, this process, which would be" documentation-lite" could be completed in a matter of days and at very low cost.

Recommendation:

That the L B Bromley Pension Fund consider investing in FIDA with an initial investment of £5.0m, funded from the existing Fidelity UK Aggregate Bond Fund, followed by quarterly transfers (amounts to be confirmed on a quarterly basis and dependent on investment performance and additional investors joining the fund).

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Document is Restricted

This page is left intentionally blank