Brent	**Pension Fund Sub-Committee** 24 February 2015 **Report from the Chief Finance Officer**
For Information	Wards Affected: ALL
Quarterly monitoring report on fund activity	

1. SUMMARY

1.1 This report provides a summary of the Fund's activity during the quarter ended 31 December 2014. It examines the economic and market background, and investment performance, as well as commenting on events in the quarter. The main points arising are:

a) The Fund has increased in value by 2.4% from £609.0m to £623.8m during the quarter ended 31 December 2014. The Fund's investment return of 2.1% under-performed its quarterly benchmark of 2.3%. During the quarter, Sterling fell by 3.9% against the US dollar. This change in currencies must be taken into consideration given the sizable non-Sterling holdings in the fund, which are not hedged against movements in sterling.

b) The single-largest contributor to this positive return during the quarter was again Global Equities (ie. excluding the UK). The quarter proved to be turbulent another turbulent quarter for equity markets.

c) The main disappointment was the Total Return Bond Fund, which lost money against the backdrop of a record-setting bull market in bonds.

d) The Global Emerging Markets equity fund also lost 2.7%, more than the 0.7% market drop, hurt by their exposure to cyclical sectors which appeared to be cheap but which have been value traps, so far.

e) Stripping out the translation effect of a weaker Sterling, only Alinda Partners beat their benchmark in 4Q14.

f) The 12-month return as at 30 December 2014 was 6.8%, marginally lower than the benchmark return of 7.2%.

g) The Fund return for the 3 years ended 30 December 2014 is an annualised 9.5% p.a., which again lags the benchmarked return of 9.9%.

h) The investment performance of the Brent Pension Fund in comparison to its benchmark for the period ended 30 December 2014 is shown below:

	Total Fund Return	Fund Benchmark Return	Local Authority Average
1 year	6.8 %	7.2%	N/A
3 years	9.5%	9.9%	N/A
5 years	7.2%	7.6%	N/A

2. RECOMMENDATIONS

2.1 Members are asked to note the investment report.

3. DETAIL

Economic and market background – quarter ended 31 December 2014

3.1 The market pressures which had been building through 2014 finally surfaced in 4Q14, with the collapse in the oil price, which took down the Russian ruble as well as other emerging market currencies. The key reason behind this was a global debt and currency mismatch. Unsustainable prices and pressures had been masked by Central Banks' policies; the events of 4Q14 refocused markets on the hitherto remote possibility that Central Bankers are fallible. This fear was reinforced by the dramatic revaluation of the Swiss Franc, after the Swiss National Bank relented to market pressure, and gave up its attempts to peg the Franc to the euro.

3.2 During the quarter ended 31 December 2014, the UK's FTSE 100 fell by 0.8%., negatively affected by the heavy weight of oil and commodities in the index. As the quarter proceeded, it was increasingly clear that the domestic economy's growth was slowing, as export markets slowed and the housing market cooled.

3.3 In the US, the strong USD weighed on international earnings. Earnings continued to benefit from lower energy prices (shale, international demand shortfall and an supply glut in oil). Jobs "onshoring" is likely to prove a continued boost. Economic headlines continued to paint a healthier economic picture than was supported by the underlying detail.

3.4 The collapse in energy prices had a dramatic (if predictable) effect on inflation expectations. This, combined with low levels of aggregate demand was enough to tip the eurozone into deflation, thereby increasing expectations of QE in the eurozone. It was therefore no surprise that government bonds and investment grade credit performed well. In Europe, long duration, high quality bonds recorded a negative yield, symptomatic of a world that was awash with liquidity, but lacked inflation, demand and confidence. Three European Central Banks implemented a negative overnight deposit rate.

3.5 Data from the Eurozone went from mixed to poor, but negative news was again largely viewed as a reason for further unconventional policy measures by the ECB, and therefore “bad” news did not dent trading sentiment. Share price gains were largely negated by the weakening euro.

3.6 Emerging markets had another tough quarter. The asset class is traditionally viewed as a geared play on global monetary conditions. Many emerging markets were impacted by the well-flagged problem of bourses’ and currencies’ sensitivity to US dollar strength. Russia’s plight was the most dramatic manifestation of this.

3.7 A market review for the quarter ended 31 December 2014, written by the Independent Financial Adviser, is attached.

Investment performance of the Fund

3.8 The investment performance of the Brent Pension Fund in comparison to the WM Local Authority percentile average for all Local Government Pension Schemes (LGPS) funds nationally is shown below:

	Period ended 30 Sept 2014	Period ended 30 Dec 14
1 year	63rd	80th
3 years	95th	87th
5 years	97th	97th
10 years	100th	100th

3.9 The comparative statistics show that the Fund has been one of the lower performing LGPS funds for a period of many years.

3.10 The Fund has under-performed over the past few years, largely due to its lower weighting in equities (49% of the fund, compared to the Local Authority average of 63%). As equity markets have become less buoyant, this has become less of a reason for under-performance.

3.11 The main reason for poor performance in 2014 was the low return of the Total Return Bond Fund. The 16% fund weighting is material and the short duration of the portfolio meant that this holding largely missed out on record government bond price gains.

3.12 The large weighting in the Private Equity Fund of Funds has been a contributor to the fund’s underperformance in recent years. In 2014, these assets benefited from currency movements and performed in line with expectations.

3.13 Table 1 shows the changes in asset allocation, how asset allocation compares with the benchmark and with the average fund (WM Local Authority average), and how the change in the market value during the quarter is allocated across asset classes. Items marked (*) in columns 4 and 8 cannot be separately analysed, but are included within the relevant asset class.

Table 1: Asset allocation as at 31 December 2014 compared to the benchmark

Assets (1)	Market Value 30/9/14 £M (2)	Market Value 30/9/14 % (3)	WM LA Average 31/12/14 % (4)	Fund Benchmark 31/12/14 % (5)	Market Value 31/12/14 £M (6)	Market Value 31/12/14 % (7)
Fixed Income						
Henderson – Total Return Bond Fund	85.5	14.1	16.9	15.0	84.2	13.5
Equities						
UK – Legal & General	86.3	14.2	26.4	15.0	86.7	13.9
UK - Smaller Companies Fund Henderson	26.1	4.6	*	4.0	25.8	4.1
O/seas – developed Legal & General	144.0	23.7	32.9	24.0	151.7	24.3
O/seas – emerging Dimensional	40.1	6.6	5.4	8.0	38.9	6.2
Property						
Aviva	36.0	5.9	7.9	8.0	36.7	5.9
Private Equity						
Capital Dynamics	78.3	12.8	3.9	10.0	82.6	13.2
Yorkshire Fund	1.1	0.2	*		1.1	0.2
Infrastructure						
Alinda	23.8	3.9	1.8	6.0	27.0	4.3
Capital Dynamics	15.6	2.6	*		9.4	1.5
Henderson PFI Fund II	1.3	0.2	*		1.3	0.2
Pooled Multi Asset						
Baillie Gifford DGF	46.8	7.7	1.9	8.0	67.1	10.7
Cash	23.8	3.9	2.9	2.0	12.2	2.0
Total	**607.0**	**100.0**	**100.0**	**100.0**	**623.8**	**100.0**

3.14 The independent WM Company measures the returns on the Brent Pension Fund. Table 2 sets out returns for the periods to 31 December 2014.

Table 2: Investment Returns in Individual Markets

Investment Category	RETURNS						Benchmark/ Index Description
	Quarter Ending 31/12/14			Year Ended 31/12/14			
	Fund %	Benchmark %	WM Local Auth %	Fund %	Benchmark %	WM Local Auth %	
Fixed Income							
Total Return Bond Fund Henderson	-1.4	1.5	-0.2	1.2	6.0	4.8	Absolute return 6% p.a.
Equities							
UK – Legal & General	0.6	0.6	0.9	1.3	1.2	0.8	FTSE All Share
UK - Small Companies Henderson	-1.2	-0.9	*	-0.0	2.7	*	FTSE Small Cap
O/seas – developed Legal & General	5.4	5.4	3.7	12.7	12.7	9.2	FTSE Dev World ex UK
O/seas – emerging Dimensional	-2.7	-0.7	0.2	1.4	3.9	8.7	MSCI Emerging Markets
Property							
Aviva	3.1	4.6	*	10.3	17.2	*	IPD All Properties Index
Private Equity							
Capital Dynamics	1.9	1.9	*	6.7	8.0	*	Absolute return 8% p.a.
Yorkshire Fund Managers	*	*	*	*	*		Absolute return 8% p.a.
Infrastructure							
Alinda	10.8	1.9	*	25.0	8.0	*	Absolute return 8% p.a.
Pooled Multi Asset							
Baillie Gifford DGF	0.8	1.0	*	6.0	4.0	*	Base Rate + 3.5% p.a.
Cash	0.1	0.1	*	0.1	0.5	*	Base Rate
Total	**2.1**	**2.3**	**3.1**	**6.8**	**7.2**	**8.1**	

3.15 The Fund's return of 2.1% under-performed its benchmark of 2.3% in 4Q14, and returned 6.8%, compared to its benchmark of 7.2%.

Compliance with statutory investment limits

3.17 LGPS investment regulations state that the Administering Authority shall have regard both to the diversification and the suitability of investments. The following table demonstrates full compliance when comparing the Fund's actual investment exposure with the statutory limits under regulation:

Investment	Statutory limit under regulation	Actual exposure at 31 Dec 2014	Compliant Yes / No
Any single holding	10%	3%	Yes
Unit trusts managed by any one body	35%	24%	Yes
Lending to any one borrower	10%	Nil	Yes
Unlisted securities of companies	15%	Nil	Yes
Any single partnership	5%	3%	Yes
Total investment in partnerships	30%	19%	Yes

Outstanding contractual commitments

3.18 The Brent Pension Fund has not entered into any new investments in private equity/infrastructure since November 2011 and whilst significant capital call payments have been made over the past two years, the outstanding contractual commitments on existing investments continue to remain significant as follows:

	31 March 2013 £'000	30 Sept 2014 £'000	31 Dec 2014 £'000
Capital Dynamics	54,077	30,404	28,524
Alinda	10,636	3,231	2,564
Yorkshire Fund Managers	266	0	0
Total	**64,979**	**33,632**	**31,088**

3.19 These outstanding investment commitments mean that the Fund needs to retain a sizeable cash balance to meet capital call payments as they arise. It also prevents the Fund from moving to its strategic allocations in Property and limits the extent to which any new investments can be considered at the present time.

4. ESTABLISHMENT OF PENSION BOARDS

4.1 Brent Council is required by statutory regulations to establish a Pensions Board. The decision to form Pensions Boards came out of The Independent Public Service Pensions Commission.

4.2 The Board will be advisory only, and will not alter the role of the Council's Pension Fund Sub-Committee.

4.2 The Board's mandated role is to provide a scrutiny function of the work of the Sub-Committee, with regards to compliance with regulations, compliance with legislation (existing and new), and to oversee the governance and administration of the Pension Fund.

4.3 The Pensions Board is required to be established by 1st April 2015 and be operational by 30th July 2015. The Board will have an equal number of employer and scheme member representatives and an independent chair. The Board will meet at least twice a year, and will be funded by the Pension Fund. The General Purposes Committee will determine the arrangements for the establish of the Pensions Board at its meeting on 25 February 2015.

5. UPDATE ON LONDON COLLECTIVE INVESTMENT VEHICLE (CIV)

5.1 Some 30 of London's 33 Authorities have signed up to the CIV. Much of the infrastructure has been put into place; in December 2014, an Asset Service Provider (Northern Trust) was appointed. Much of the work carried out by London Councils and the Technical Sub Group (TSG) is now focused on preparing the application to the Financial Conduct Authority (FCA).

5.2 The initial deadline of May 2015 has slipped, due to the plethora of complex technical and legal issues. The aim is to launch in summer 2015. The FCA application is the key swing factor in terms of precise timing.

5.3 Negotiations with fund managers are ongoing. It is envisioned that at the time of launch, passive managers will be included, with select active equity and bond managers (there is considerably less overlap of active bond managers within London than there is with active equity managers). The main cost savings will be in the alternatives space, and these will take the longest period of time to develop for the CIV.

5.4 It remains unclear what the final outcome of the latest Government Consultation over LGPS reform will be, given the national political cycle. If successful, the CIV will address many of the issues raised during the Consultations process.

6. FINANCIAL IMPLICATIONS

6.1 These are included within the report.

7. DIVERSITY IMPLICATIONS

7.1 None.

8. STAFFING IMPLICATIONS

8.1 None.

9. LEGAL IMPLICATIONS

9.1 None.

10. BACKGROUND INFORMATION

10.1 Henderson Investors – September 2014 quarter report
Legal & General – September 2014 quarter report
Dimensional Asset Management – September 2014 quarter report

Baillie Gifford – September 2014 quarter report

11. CONTACT OFFICERS

11.1 Persons wishing to discuss the above should contact the Investment and Pensions Section, on 020 8937 1472 at Brent Civic Centre.

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QUARTERLY REVIEW PREPARED FOR

Brent Council Pension Fund

Q4 2014

20 January 2015

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BRENT COUNCIL PENSION FUND
Quarterly Review, October – December 2014

Economy

1. The US economy showed strong growth of +1.2% in the third quarter, while the UK's 0.7% gain was partly offset by downward revisions to earlier quarters. The Eurozone economies remained sluggish, while Japan contracted for a second successive quarter and China's growth rate looked likely to slow down. The fall in oil prices reduced rates of inflation globally, but whereas the annual UK core rate (excluding energy, food and alcohol) was +1.3%, the negative inflation in the Eurozone was symptomatic of weak demand in the region.

(In the table below, bracketed figures show the forecasts at the time of the previous Quarterly Review in October)

[Source of estimates: The Economist, January 10th, 2015]

Consensus real growth (%)					**Consumer prices latest (%)**
	2012	**2013**	**2014E**	**2015E**	
UK	-0.1	+1.7	+2.9 (+3.1)	+2.7	+0.5 (CPI)
USA	+2.2	+1.9	+2.3 (+2.2)	+3.1	+1.3
Eurozone	-0.5	-0.4	+0.8 (+0.8)	+1.1	**-0.2**
Japan	+1.9	+1.7	+0.3 (+1.0)	+1.0	+2.4
China	+7.8	+7.7	+7.3 (+7.3)	+7.0	+1.4

2. In his **Autumn Statement** on December 3rd, George Osborne forecast UK GDP growth of 3.0% in 2014, but the estimates for the following five years were slightly lower than previously forecast, and all below 2.5%. CPI inflation is expected to remain in the 1-2% range throughout 2015 and 2016. The fiscal deficit in the 2014/15 tax year is expected to be £91.3bn (5% of GDP, and some £5bn larger than previously forecast) and to fall each year until a surplus of £4bn is achieved in 2018/19. The Debt/GDP ratio was forecast to peak at 81% in 2015/16. Notable changes announced in the Statement included an immediate revamp of Stamp Duty rates, and restrictions on the banks' ability to offset past losses against future tax.

3. The coalition's planned reduction in the fiscal deficit is predicated on cutting public spending by <u>1% of GDP</u> each year, while increasing tax receipts by 0.1% of GDP each year. The Labour Party criticised the scale of these spending cuts, and indicated that, if elected, they would cut spending by only <u>0.6% of GDP</u> per annum. This difference in approach looks likely to be one of the main themes of the forthcoming General Election campaign.

4. Towards the end of October, the US Federal Reserve confirmed that it would end its purchases of bonds under the Quantitative Easing programme. Only a day later, the Bank of Japan announced it would step up its QE operation, with the aim of increasing Japan's monetary base to Y80 trn (compared with the previous target of 60-70trn), primarily by purchasing Japan Government Bonds. In mid-November, Japan's GDP for the second quarter was announced to be – 0.4%, thereby confirming a recession, and shortly afterwards Prime Minister Abe announced he would defer the second stage of the consumption tax increase from October 2015 to April 2017. He also called a snap election for December 14th, which, in the face of opposition disarray, confirmed the LDP's standing in the Diet.

5. The most dramatic – and unexpected – development has been the steep fall in the price of **oil**. A barrel of Brent Crude halved in price (from \$112 to \$57) during the second half of 2014, and has fallen to below \$50 in the first two weeks of January. The causes have been a mix of slowing demand and inflexible supply. Within the OPEC group, the low-cost producers (Saudi Arabia, Kuwait, Qatar and UAE) have decided to maintain their production levels, knowing that this will force the price of oil downwards. Their motivation may be to make life difficult for the shale oil producers of North America, whose profitability – and in some cases viability – is severely affected by such a sharp reduction in market prices. While cheaper fuel is beneficial for private and industrial consumers, it is deeply negative for countries relying on oil exports, notably Russia, Nigeria and Venezuela.

6. The plunging oil price dealt a further blow to the **Russian** economy, already weakened by the imposition of trade sanctions earlier in the year. After raising interest rates from 9.5% to 10.5% on December 11, ostensibly to combat inflation, the Russian Central Bank suddenly increased the rate to 17% at midnight on December 15, in an attempt to defend the rouble which had fallen to R66 per \$. The following day the rate fell further - to 77 per \$ - before rebounding to the 55 level on heavy buying from the Russian Central Bank. By mid-January the rouble was trading at 65 per \$.

7. The political situation in **Greece** has reawakened concerns about the future of the Eurozone. On December 29th the Greek parliament failed to elect a president, forcing an early election which is set for January 25th. This could bring in a new government of the far-left populist party Syriza, led by Alexis Tsipras. He has advocated revoking most of the conditions attached to Greece's bail-out: he would end austerity, scrap asset sales and seek to repudiate much of Greece's debt. This agenda would be inconsistent with Greece's continuing membership of the Euro, and investors have reacted to this prospect with heavy selling of Greek shares and government bonds.

8. On January 15th the **Swiss** National Bank surprised markets with the news that it was abandoning the currency cap against the Euro, which had prevented the Swiss Franc appreciating beyond SFr1.20 per € since 2011. A massive surge in the Swiss Franc took it to 0.85 /€, before it closed the day at 1.04/€ and strengthened to 0.98/€ on Jan 16th.

Deprived of support from the SNB, the Euro weakened to $1.15 – its lowest level for eleven years. In two days the £ moved from SFr 1.55 to just SFr 1.29.

Markets

9. The movements of **equity** market indices for the quarter as a whole conceal a volatile period, where prices fell by some 10% in the month to mid-October (as described in my previous report), before recovering, and then underwent a smaller correction in early December. UK, European and Emerging Markets lagged the other regions, while almost the entire gain in the All-World Index was attributable to North America's rise.

	Capital return (in £, %) to 31.12.14		
Weight %	Region	**3 months**	**12 months**
100.0	FTSE All-World Index	**+4.0**	**+8.5**
54.9	FTSE All-World North America	+7.7	+17.1
7.8	FTSE All-World Japan	+1.5	+0.7
11.6	FTSE All-World Asia Pacific ex Japan	+2.7	+6.6
15.6	FTSE All-World Europe (ex-UK)	-1.7	-4.4
7.2	FTSE All-World UK	-0.8	-2.9
8.9	FTSE All-World Emerging Markets	+0.0	+4.7

[Source: FTSE All-World Review, December 2014]

10. Within the UK equity market, only the 'mid-cap' FTSE 250 Index gained ground during the quarter or, indeed, during the year as a whole.

(Capital only %, to 31.12.14)	**3 months**	**12 months**
FTSE 100	**- 0.9**	**-2.7**
FTSE 250	**+4.6**	**+0.9**
FTSE Small Cap	**-0.3**	**-1.5**
FTSE All-Share	**+0.0**	**-2.1**

[Source: Financial Times]

11. By sector, Oil & Gas and Basic Materials were dragged down by the falling prices of oil and commodities, while all the other sectors (with the exception of Telecommunications) registered solid gains during the quarter.

Capital return (in £, %) to 31.12.14		

Industry Group	3 months	12 months
Health Care	+6.7	+24.1
Technology	+6.9	+23.4
Utilities	+5.7	+15.9
Consumer Services	+10.7	+11.9
FTSE All-World	**+4.0**	**+8.5**
Financials	+5.6	+8.2
Consumer Goods	+6.4	+7.2
Industrials	+4.7	+5.8
Telecommunications	-0.1	+0.8
Basic Materials	-3.3	-5.3
Oil & Gas	-12.8	-10.9

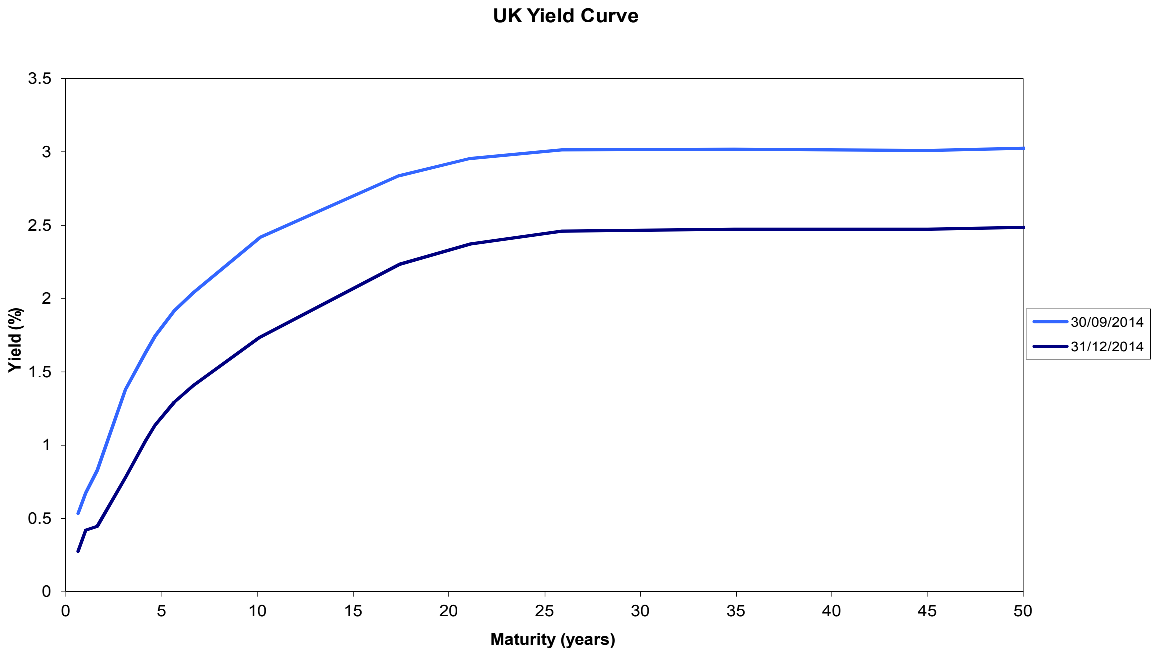
[Source: FTSE All-World Review, December 2014]

12. **Government bond** markets in the 'safe haven' economies continued to strengthen, and yields have fallen substantially during 2014 in all these markets as shown in the table below. As investors began to worry about the outlook for Greek bonds (see para 7) and possibly other peripherals, the security of German, UK or US government bonds became increasingly attractive. Lower inflation has also contributed to the demand for fixed-coupon bonds by increasing the real yields.

10-year government bond yields (%)					
	Dec 11	**Dec 12**	**Dec 2013**	**Sept 2014**	**Dec 2014**
US	1.88	1.76	3.03	2.49	2.17
UK	1.98	1.85	3.04	2.43	1.76
Germany	1.83	1.32	1.94	0.95	0.54
Japan	0.98	0.79	0.74	0.53	0.33

[Source: Financial Times]

13. In the UK, yields continued to reduce at all durations, as shown below.



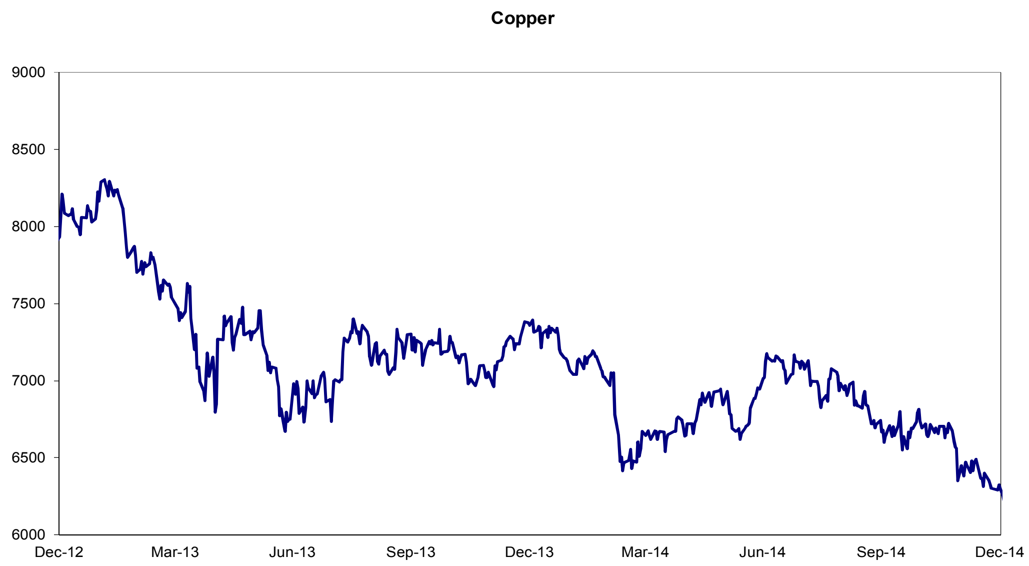
Currencies

14. The yen fell after the Bank of Japan embarked on its enhanced QE policy, while the pound fell against the dollar (see graph below) as it became clear that the first UK interest rate rise would be delayed until at least the final quarter of 2015.

	31.12.13	30.09.14	31.12.14	£ move 3m	12m
$ per £	1.656	1.621	1.559	- 3.8%	- 5.9%
€ per £	1.202	1.283	1.289	+ 0.5%	+ 7.2%
Y per £	174.1	177.8	186.9	+ 5.1%	+ 7.4%

Commodities

15. The sharp fall in oil prices has been described in para 5, but the price of copper also weakened on the expectation of lower demand from China.



Property

16. The UK property market has maintained its strong momentum of the past eighteen months, with returns, as measured by the IPD Monthly Index, especially strong in the Office and Industrial sectors.

	3-months	12-months
All Property	**+ 4.4%**	**+ 19.3%**
Retail	**+ 2.8%**	**+ 14.1%**
Office	**+ 5.6%**	**+ 24.3%**
Industrial	**+ 6.0%**	**+ 24.4%**

[IPD Monthly Index of total returns, to end-Dec 2014]

Outlook

17. The sharp fall in the oil price should be of benefit to consumers, by boosting their spendable income, and to those companies whose input costs are significantly related to the price of oil. Clearly there are other companies (e.g those reliant on oil exploration) who are suffering from the new regime, and will continue to do so while the price remains depressed. Oil-exporting countries are also under pressure, and several Emerging Markets fall into this category, just as oil-importing countries are beneficiaries. Overall, the boost to consumer spending should be positive for global economic growth in 2015.

18. In the Eurozone, all eyes are on the European Central Bank, which is expected to introduce Quantitative Easing now that the German court has declared it permissible. Of

greater immediate impact may be the outcome of the Greek election; if Syriza is successful, there could be a standoff with the European authorities on the continuation of austerity in Greece. Other peripheral European states will be watching this situation closely.

19. While the lower level of inflation makes lower bond yields more sustainable, and in turn emphasises the attractions of equity yields, there are also many reasons to remain cautious on the outlook for equities during 2015.

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January 20th, 2015

[All graphs supplied by Legal & General Investment Management]