Agenda Item:

11b

Pension Fund Committee

Dorset County Council

Date of Meeting	13 September 2017
Officer	Pension Fund Administrator
Subject of Report	**Global Equities Managers Report**
Executive Summary	The purpose of this report is to update the Committee on the performance of the Fund's Global Equities Managers as at the end of the first quarter of the 2017/18 Financial Year to 30 June 2017.
Impact Assessment:	Equalities Impact Assessment: N/A
	Use of Evidence: N/A
	Budget: N/A
	Risk Assessment: The Fund assesses the risks of its investments in detail, and considers them as part of the strategic allocation. In addition, risk analysis is provided alongside the quarterly performance monitoring when assessing and reviewing fund manager performance.
	Other Implications: None

Recommendation	That the Committee : i) Review and comment upon the performance of the Fund's Global Equities managers.
Reason for Recommendation	To ensure that the Fund has the appropriate management arrangements in place and are being monitored.
Appendices	None
Background Papers	Quarterly manager reports.
Report Originator and Contact	Name: David Wilkes Tel: 01305 224119 Email: d.wilkes@dorsetcc.gov.uk

1. Background

1.1 With effect from mid December 2015, the Fund replaced its then two global equities managers, Pictet Asset Management and Janus Intech, with three new managers, Allianz Global Investors, Investec Asset Management and Wellington Investment Management.

2. Valuation

2.1 The table below summarises the valuations for the three managers as at 1 April 2017 and 30 June 2017.

	Allianz	Investec	Wellington	Total
	£000s	£000s	£000s	£000s
Valuation 01-Apr-17	270,886	193,966	206,868	671,720
Investment	-	-	-	-
Distribution	-	-	-	-
Increase in Valuation	- 856	925	1,422	1,490
Valuation 30-Jun-17	270,030	194,891	208,290	673,210

2.2 No additional investment or distribution has been made with the three managers in this financial year.

3. Performance

3.1 The table below summarises the performance for each manager in absolute terms and compared to their respective benchmarks for the quarter, the 12 months and since inception to 30 June 2017.

	Allianz	Investec	Wellington
Quarter to Date			
Performance	-0.7%	0.5%	0.2%
Benchmark	0.1%	0.1%	0.1%
Relative Return	-0.8%	0.4%	0.1%
Twelve Months to Date			
Performance	21.4%	22.4%	23.2%
Benchmark	21.6%	21.6%	21.6%
Relative Return	-0.2%	0.8%	1.6%
Since Inception			
Performance	20.8%	21.0%	22.4%
Benchmark	21.1%	21.1%	21.1%
Relative Return	-0.3%	-0.1%	1.3%

3.2 Investec and Wellington both outperformed their benchmarks for the three months to 30 June 2017 by 0.4% and 0.1% respectively, whilst Allianz underperformed by 0.8% over the same period. Since inception, Wellington has outperformed its benchmark by 1.3%, whilst Allianz and Investec underperformed their benchmarks by 0.3% and 0.1% respectively.

4. Market Review

4.1 Global equities made modest progress throughout the first quarter, with many markets touching record highs amid growing optimism over the outlook for global growth. Most sectors advanced, with the healthcare and information technology sectors posting the strongest performance, but energy stocks retreated as oil prices slid to their lowest levels this year.

4.2 US equities increased during the quarter, reaching a series of new highs to end the period with modest gains as sentiment was boosted by strong corporate earnings growth. However, the rally appeared to slow towards the end of June amid concerns that President Trump's administration may struggle to implement tax reforms and other key election promises. Political risk also weighed on sentiment as President Trump faced claims he tried to interfere with the FBI's investigation into formal national security advisor Michael Flynn.

4.3 European equities rallied modestly over the quarter, boosted by Emmanuel Macron's decisive victory in the French presidential election and by signs that the Eurozone's economic growth was continuing to pick up momentum. However, strong initial gains were alleviated in June following more hawkish comments from the European Central Bank.

4.4 Most equity markets in the Pacific ex Japan advanced over the quarter, although returns for the region as a whole were hindered by a weak performance from Australia, the region's largest market. Australian equities fell to a four month low in early June due to negative returns from the banks which were hit by government plans to impose a tax on their balance sheet liabilities.

4.5 Japanese equities rallied strongly over the quarter, boosted by generally positive economic news. While Japan's first quarter GDP growth was revised down to 1.0% on an annual basis, from an initial estimate of 2.2%, this was mainly due to an unexpected decline in oil inventories, meaning that the underlying pace of growth was not affected.

4.6 Emerging market equities rallied strongly over the first quarter, outperforming many developed markets, buoyed by optimism over the outlook for the global economy, signs of an improvement in economic activity in China and a weaker US dollar.

Manager Commentaries

5. Allianz

5.1 It was a mixed quarter for global investment styles and the portfolio, which saw a negative return of 0.68%, underperforming the benchmark by 0.82%. The weakness in the investment style Value was too strong to be compensated by the rather limited relative performance contribution of our further investment styles.

5.2 Sector allocation added to the relative performance largely driven by strong relative performance (+11 bps) from being underweight in the Energy sector. Single stock selection was particularly weak in Information Technology (-46 bps), Consumer Discretionary (-27 bps) and Consumer Staples (-26 bps), while stocks selected within the Energy Sector added to relative performance by 39 bps.

5.3 Regional allocation made a minor contribution of 1 bp, mostly due to the underweight position in Europe ex UK which detracted by 7 bps offsetting the overweight. This was more than compensated by the successful overweight position in the Eurozone (+3 bps) and the underweight position in Pacific ex Japan (+ 4 bps) which were both beneficial.

5.4 The quarter had been a mixed environment for global investment styles and the portfolio overall. The most prominent investment style Value, alongside other more risk-on, cyclical investment styles like Small Caps and High Risk underperformed the more risk-off, non-cyclical investment styles like High Quality and Stable Growth which performed positively. Trend following investment styles also delivered positive performance in the quarter, with Price Momentum strategies doing well while earnings revisions strategies were trailing the benchmark. Overall, the weakness in Value and Earnings Revisions could not be offset by the rather limited relative performance contributions from Quality, Price Momentum and Stable Growth.

6. Investec

6.1 The performance of Investec’s Four Factors approach provided a tailwind for portfolio performance in the quarter. The strategy and technical factors had a strong sector, while the earnings and value factors were weaker. Relative performance in the quarter was led by favourable stock selection in financials, information technology and materials. The overweight position in information technology since the start of the year was now being shown to be a positive. On a regional basis, stock selection in Asia Pacific ex Japan and the US made a strong positive contribution to relative returns, while stock selection in the UK and Japan was negative.

6.2 In financials, Asian stocks were among the strongest positive contributions to relative returns, with the sector as a whole benefiting from more hawkish news on monetary policy from central banks. Bank of China performed strongly, while the pan-Asian life insurance company AIA also made gains on the quarter due to good underlying results.

6.3 The selections within the IT sector were among the leading stocks over the quarter, starting with American online payments operator PayPal, which reported strong quarterly results with continued transaction volume growth and limited impact from the recent deals done with Visa and Mastercard. The company’s mobile payment service Venmo also continues to show promising growth. US semiconductor manufacturer Lam Research also added to relative returns, amid strong positive sentiment in the technology sector ahead of Apple’s anticipated product launch in the year, which is expected to benefit firms in its supply chain.

6.4 On a sector level, industrials, healthcare and consumer discretionary detracted. US electronics distribution and services company Wesco was a negative to performance as shares suffered following a negatively received investor day and concerns that increased competitive pressures would adversely affect pricing trends also weighed on the stock. The holding in US media giant CBS gave up some of its gains after a multi-month advance despite delivering a solid set of earnings result that were ahead of expectations. Healthcare exposure was a net detractor with Shire’s share price retreating in the quarter, primarily due to concerns about the pharmaceutical company’s haemophilia franchise.

7. Wellington

7.1 During the quarter, the Global Research Equity Portfolio outperformed the Index with eight of the eleven sectors adding value. Stock selection within information technology, real estate and industrials were the primary contributors to relative outperformance while stock selection in energy and healthcare offset some of these gains.

7.2 Within information technology, Arista Networks and ServiceNow were among the top contributors this quarter. Arista Networks, a supplier of cloud-computing switches and other services, continued its strong momentum from the previous quarter and delivered strong earnings results. ServiceNow, a US-based cloud-computing company, delivered healthy first quarter results expanding operating margins.

7.3 Real estate boosted relative performance in this quarter. American Tower, an owner and operator of wireless and broadcast communications infrastructure, reported a good quarter with clear acceleration in tenant demand. US leasing activity was strong and the company's international growth remains steady.

7.4 In industrials, the overweight exposure to XPO Logistics, a truck broker and third party logistics company, contributed to relative returns. Given the stock's strong performance, it looks relatively less attractive against peers, and with greater risk of disintermediation and price compression, the stock will be carefully monitored.

7.5 Energy weighed on relative results this quarter. Newfield Exploration, an exploration and production company, reported strong results with earnings and cash flow ahead of expectations. However, despite improvements in operations, oil price uncertainty has weighed heavily on not only Newfield, but other exploration and production companies as well.

7.6 MEG Energy, a Canadian oil-sands company, detracted from relative returns. Oil sands remain relatively high cost in terms of bringing new projects online, but once built, the all-in cost of running them is relatively low as these are mines and not wells that must be drilled over time. These upfront costs of these mines have caused investor scepticism, but with a recovery in oil, the company stands to do well.

7.7 Healthcare was also a weaker area of the portfolio this quarter. The portfolio's lack of exposure to Novartis detracted from relative results as did the overweight exposure to UCB, a Belgium based pharmaceutical company. The company announced that the Food and Drug Administration will further analyse the data and a previously filed study, which will push out the US approval decision until 2018. There are investor concerns on this near-term disappointment are overdone and therefore this stock has been added to the portfolio.

Richard Bates
Pension Fund Administrator
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