REVIEW ON PERFORMANCE MEASUREMENT OF THE PENSION FUND

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Papers with this report	Northern Trust Executive Report WM Local Authority Annual and Quarter Reports Private Equity Listing Private Equity reports from Adams Street and LGT

SUMMARY

This report reviews the fund management performance for the London Borough of Hillingdon Pension Fund for the quarter to 30 September 2009. The value of the fund as at the 30 September was £517m.

RECOMMENDATIONS

1. **That the content of this report be noted and the performance of the Fund Managers be discussed.**

INFORMATION

1. The performance of the whole fund for the quarter to 30 September 2009 showed an outperformance figure of 0.08% with positive returns of 17.40%, compared to the benchmark 17.31%. Over the longer term, one year, five year and since inception figures show a slight improvement on the previous quarter but remain below the benchmark by 1.51%, 1.86% and 0.26% respectively.

Performance Attribution

	Q3 2009 %	1 Year %	3 Years %	5 Years %	Since Inception %
Goldman Sachs	1.17	(0.48)	(1.12)	(0.68)	(0.80)
UBS	1.93	1.17	(1.72)	(1.61)	1.31
Alliance Bernstein	(0.41)	(4.88)	(3.97)	-	(3.70)
UBS Property	(0.33)	0.32	0.50	-	0.21
SSgA	0.17	-	-	-	0.16
SSgA Temporary	0.09	-	-	-	-
SSgA Drawdown	0.31	-	-	-	-
Total Fund	**0.08**	**(1.51)**	**(2.40)**	**(1.86)**	**(0.26)**

2. The positive performance for this quarter was primarily derived from the weakening of sterling which added 1.90% from the resultant passive currency effect. At a total fund level stock selection and asset allocation detracted from performance, with a negative impact of 0.92% and 0.82% respectively.

3. Alliance Bernstein returned a positive 21.87% over the quarter but underperformed against their benchmark by 0.41%. The largest negative impact on performance resulted from UK stock selection and currency hedging. In contrast the overall effect of overseas stock selection added to returns as did the passive currency effect and asset allocation.

4. GSAM returned 8.26% against their benchmark of 7.09%, outperforming by 1.17%. The portfolio's cross-sector allocation strategy was the key contributor to performance with mortgage credit and corporate credit adding to results for a second consecutive quarter. Corporate security selection was also a major contributor with overweight positions in high quality banks and insurance companies having a positive impact.

5. UBS delivered a positive performance of 24.30% outperforming the benchmark by 1.93%. In overall terms stock selection added to performance with major contributions being derived from overweight positions in Prudential, British Airways, Logica, and Daily Mail. Not holding BG group also contributed. Negative impacts included overweight positions in BP, Glaxo and HMV. Other detractors included the underweight position in HSBC and not holding Standard Chartered.

6. This quarter saw a reversal in the trend of negative returns within the property asset class for the first time since Q2 2007. The portfolio delivered positive performance of 1.77% but underperformed against the benchmark by 0.33%. The high cash holding which had served the portfolio well during the property downturn detracted from results this quarter. Of the funds within the portfolio, Henderson UK Property, UBS South East Recovery, Lothbury Property, and Henderson Retail Warehouse outperformed the benchmark.

7. The requirement for SSgA as a passive manager is to replicate their performance benchmark. However efficient management across their three portfolios has resulted in modest outperformance figures for this quarter of 0.17%, 0.31% and 0.09%.

Absolute Returns

	Alliance Bernstein £000	GSAM £000	SSgA (3 funds) £000	UBS £000	UBS Property £000
Opening Balance	85,193	55,693	160,771	78,408	39,186
Appreciation	18,019	4,556	30,042	18,369	259
Income Received	616	43	-	677	437
Investment Movement	0	0	391	(109)	-
Closing Balance	103,828	60,292	191,204	97,345	39,882
Active Management Contribution	(354)	650	343	1,498	(127)

8. The above table provides details on the impact of manager performance on absolute asset values. The outperformance of GSAM and UBS and SSgA had a positive impact on the appreciation of holdings contributing £650k, £343k and

£1,498k respectively. In contrast the underperformance of Alliance Bernstein and UBS property reduced asset appreciation by £354k and 127K.

9. At the end of September 2009, £26.97m had been invested in private equity, which equates to 5.22% of the fund against the target investment of 5%. However this level still remains within the limits of the over-commitment strategy. In terms of cash movements, over the quarter £371k was called by Adams Street and £619k by LGT. In addition there was a distribution from LGT of £268K.

10. The securities lending activity for the quarter resulted in income of £18.1k. Offset against this was £6.3k of expenses leaving a net figure earned of £11.8k. The fund is permitted to lend up to 25% of the eligible assets total and as at 30 September 2009 the assets on loan totalled £28m representing approximately 14% of this total.

11. Following another positive quarter there was an improvement in the Hillingdon returns compared to the WM Local Authority summary figures. For the quarter ending 30 September 2009 Hillingdon outperformed the average by 1.40%. The one year performance figure has also improved reducing the deficit to 0.86% (Q2 2.28%).

M&G UK Companies Financing Fund - update

12. M&G expect further closings to bring the total fund value to approximately £1.6 billion and that this figure will be sufficient to gain the appropriate level of diversification needed. They will continue to bring new investors into the fund until the end of the year at which time it is expected to close.

13. Since the last update funding conditions for many companies has improved. The three main factors contributing to this are firstly, the Bank of England quantitative easing policy which is keeping government bond yields low which in turn has encouraged investment into higher yielding corporate debt. Secondly, the instruction to Lloyds and RBS to increase lending to UK companies and finally public bond markets which have welcomed new issuers who have launched bonds at much better levels than were previously experienced.

14. M&G do not feel the current funding situation is sustainable as the reduced number of available banks do not have and will not have the lending capacity as before the crisis. M&G are adamant though, they will not chase the market and make loans at rates which do not give and attractive risk rated return. M&G are approaching more companies directly and have become more aware that many target clients are not being served well by the investment banking community. It is believed the need for the fund still exists and this will become apparent over the next year when artificial liquidity dries up.

Market Commentary

15. Equity markets showed very strong returns across the globe with all regions performing positively. The general economic news was reassuring as many leading indicators pointed towards recovery. The German and French economies led the way in Europe whilst other measures showed the US also improving. The main driver for recovery is expected to come from manufacturers which are now beginning to replenish depleted inventory levels.

16. In terms of fixed income there was a slow down in the tightening of credit spreads however, yields on corporate debt, high yield issues and emerging market debt all reduced providing positive returns.

17. UK commercial property values showed signs of stabilisation during the third quarter and as confidence returned to the market there was a substantial rally in forward looking real estate products.

FINANCIAL IMPLICATIONS

These are set out in the report

LEGAL IMPLICATIONS

There are no legal implications arising directly from the report

BACKGROUND DOCUMENTS

None