ITEM 6

NORTH YORKSHIRE COUNTY COUNCIL

PENSION FUND COMMITTEE

22 SEPTEMBER 2011

PERFORMANCE OF THE FUND'S PORTFOLIO FOR THE QUARTER AND YEAR ENDING 30 JUNE 2011

Report of the Treasurer

1.0 **PURPOSE OF REPORT**

1.1 To report the investment performance of the overall Fund, and of the individual Fund Managers, for the Quarter to 30 June 2011 and the twelve months ending on that same date.

2.0 **PERFORMANCE REPORT**

2.1 The report (**enclosed as a separate document**) produced by Mellon Analytical Solutions (MAS) provides a complete performance analysis of the North Yorkshire Pension Fund for the quarter and year ending 30 June 2011.

2.2 Using the format prepared by MAS the report highlights the performance of the total Fund by asset class against the customised Fund benchmark. There is also an analysis of the performance of each manager against their specific benchmark and a comparison of performance levels over time.

3.0 **PERFORMANCE OF THE FUND**

3.1 The performance of the various managers against their benchmarks for the Quarter ended 30 June 2011 is detailed on **pages 4 / 5** of the MAS report. This performance is measured on a time-weighted basis and expressed as a +/- variation to their benchmark.

3.2 **The absolute overall return for the quarter (+1.8%) was below the customised benchmark (+2.2%) by 0.4%.**

3.3 **Over the rolling year the Fund performance was 1.7% above the customised benchmark. The 12 month absolute rolling return of + 23% is a relatively high figure compared to previous annual rolling returns throughout the 2010/11 year. Absolute returns over the six months to 31 December 2010 and 30 June 2011 were +19.2% and +3.2% respectively.**

3.4 These figures represent satisfactory performance with the Fund outperforming its benchmark in three out of the last four quarters. Manager performance produced a mixture of positive and negative relative returns, with equity managers positive and fixed income managers negative. Following the end of the June 2011 quarter investors reacted badly to the Euro zone response to the debt crisis and the length of time it took to increase the US debt ceiling. Financial markets remain unpredictably vulnerable to world events. It is therefore still essential to try and understand, and assess,

- the potential for further turbulence in the financial markets
- the ongoing appropriateness of the investment strategy of the Fund (which was designed to operate in "normal" financial market conditions)
- the performance of individual fund managers in these unstable market conditions

It is also critical to understand the timescale over which any or all of these factors may impact on the future performance of the Fund.

3.5 With this in mind the Appendices used in this report have been designed to present a fuller picture of the reasons behind the recent investment performance.

3.6 The content of these Appendices is now as follows.

Appendix 1	Fund Manager Performance over the three years to 30 June 2011 in absolute percentage terms
Appendix 2	Performance of NYPF relative to other LGPS Funds
Appendix 3	Solvency position (in % and £ terms) since the 2001 Triennial Valuation; this Appendix also shows in absolute terms the +/- in the value of assets and liabilities of the Fund
Appendix 4	Solvency graph – this shows the key figures from **Appendix 3** in a simple graphical format
Appendix 5	Solvency of NYPF relative to other County administered LGPS Funds at the 2010 Valuation illustrating the legacy of reduced contribution rates in the 1990s
Appendix 6	Solvency of NYPF illustrating the legacy of reduced contribution rates in the 1990s
Appendix 7	Details of Rebalancing @ 30 June 2011

3.7 The separate reports of the Investment Adviser and Investment Consultant explain what has been happening in the financial markets, and what may happen in the short, medium and longer term.

4.0 FUND MANAGER PERFORMANCE

4.1 In monetary terms the positive absolute return of +1.8% in the Quarter increased the invested value of the Fund by £26.9m. However, taking into account new money, the value of the Fund increased by £28.5m. In absolute terms this movement is primarily attributable to capital gains made by Standard Life (£14.8m) and Amundi (£5.7m).

4.2 Absolute performance in percentage and cash terms is shown in the following table.

	absolute performance (%)					absolute performance (£)	
	q/e Sep 2010	q/e Dec 2010	q/e Mar 2011	q/e Jun 2011	y/e Jun 2011	q/e Jun 2011	y/e Jun 2011
Baillie Gifford : Global Equities	11.2	9.9	2.3	0.7	25.9	1.8	52.0
Baillie Gifford : LTGG	12.8	8.9	6.6	0.7	31.8	1.1	39.7
FIL Inv Ser UK : Global Equities	8.6	9.7	2.1	0.6	22.3	2.2	65.1
Standard Life : UK Equities	18.2	10.1	-2.4	4.8	33.1	17.6	95.9
Equities sub-total						22.7	252.7
Amundi AM : Global Bonds	3.8	0	0.8	2.6	7.4	5.7	13.5
European Credit Mgmt : Global Bonds	5.2	1.3	2.9	-0.1	9.5	-0.1	10.0
Fixed income sub-total						5.6	23.5
RC Brown Investment : UK Equities	15.5	2.4	3.9	3.6	27.3	0.1	0.5
Movement in cash reserves						0.1	32.6
Movement in Fund Investments and Cash						28.5	309.3

Cumulative absolute performance by each manager over the last three years in percentage terms is illustrated at **Appendix 1**.

4.3 Positive absolute performance was achieved by most Managers with only one manager producing a negative return. Market volatility during the quarter was low but reached the levels experienced in 2008 in the following weeks. This and other issues are further discussed in the report of the Investment Adviser.

Performance relative to other LGPS Funds

4.4 **Appendix 2** shows the **performance of NYPF relative to other Funds in the LGPS universe**. Performance is above the Local Authority average in the quarter by 0.1% and was also ahead for the 12 month period to June 2011 (+5.2%). NYPF has shown a strong and consistent correlation to the performance of other LGPS funds over the last 10 years in almost every quarter.

After being ranked as the best performing Local Authority Fund in 2009 as measured by WM Performance Services NYPF was placed in the top quartile three times in 2010 and once in the bottom quartile, and was the 8th best performer over the year. The impressive ranking was largely attributable to equities rather than bonds. The Fund was ranked in the second quartile for the March 2011 and June 2011 quarters.

Overseas Equities

4.5 **Fidelity** produced a positive relative return in the quarter (+0.1%) against a benchmark return of +0.5%. Performance over the year to June 2011 was also positive (+0.2% relative), but since inception in November 2008 is 0.3% below the benchmark. The manager has reported that performance during July and August has been slightly behind the benchmark.

For the fourth quarter in a row, Fidelity reported relative performance exceeding the benchmark in two regions (Europe (ex UK), Asia Pacific). There has been a negative contribution from Emerging Markets in each quarter over the same period and this allocation has underperformed the benchmark by 6.9% over the year to 30 June 2011. Recent changes to the management of this pooled fund have taken place in an attempt to address the issue.

4.6 The Global Alpha fund managed by **Baillie Gifford** produced a positive relative return for the tenth quarter in succession further extending an already exceptional run of out-performance.

The LTGG fund, also managed by **Baillie Gifford** produced a positive relative return. The Fund has outperformed the FTSE All World benchmark in every quarter except one, since 2007.

4.7 Both funds managed by Baillie Gifford have produced sustained outperformance. Global Alpha and LTGG are 1.9% and 3.4% respectively ahead of the FTSE All World benchmark, since inception in September 2006 and focus on long term time horizons for performance purposes, broadly three to five years. However, although losses have been suffered in absolute terms since the June 2011 quarter, relative performance has been positive.

UK Equities

4.8 **Standard Life** produced a positive relative return (+1.2%) in the quarter against the FTSE 350 equally weighted benchmark return of +3.6% recovering some of the losses suffered in the previous quarter. Relative performance for the year was 3% above the benchmark representing welcome news, however volatility continues to be a significant issue.

Since the end of the quarter relative performance has been poor, however the manager believes this is due to the negative view markets have taken on the macro economic outlook leading to a lack of confidence which does not reflect company fundamentals, and expects the losses to be recovered as markets return to normal.

4.9 The ethical equity portfolio operated by **R C Brown** outperformed the FTSE All Share by 1.7% over the quarter and was positive over the rolling 12 month period (+1.7%).

Fixed Income

4.10 **ECM** produced -0.1% against the cash benchmark for the quarter. A slowdown in global growth indicators over the last 6 months and the dramatic events in Greece led to falls in corporate bond indices as investors fled to safer havens. For the year to June 2011 the fund was 9.3% ahead of the cash benchmark. Credit markets have performed badly since the June 2011 quarter end and the manager was negative in absolute terms for the first eight months of 2011, although ahead of comparable credit indices by 1.8%. The manager will be presenting to the Committee on 23 September when performance and other issues can be explored.

4.11 Between July 2005 and May 2007 NYPF invested £125m with ECM. The valuation reached a peak of £141m in December 2007, dropped to a low point of £58m in February 2009, and by the end of June 2011 stood at £116m.

4.12 **Amundi** was below the benchmark by 1.9% in the quarter. The retreat of global government bond markets and poor performance by the Financials sector were significant contributors. Three out of the last four quarters have been negative with performance over the last 12 months being below the benchmark by 1.8%. However the manager was positive in absolute and relative terms over July and August despite the difficult market conditions.

4.13 These results give a combined relative performance (as reported by MAS) in global fixed income of -2.9% in the quarter.

5.0 RISK INDICATORS

5.1 As reported to the May 2011 PFC meeting, the MAS Performance Report (**pages 12 to 13**) includes three long-term risk indicators.

5.2 The Fund's annualised **Standard Deviation** for the rolling three year period to June 2011 (23%) is higher than the average over the three year period to June 2010 (22%). This shows the unprecedented level of volatility of the Fund's return over recent years which is not surprising given the recent market conditions. Before the financial markets crashed in 2008 the figure was around the 6-7% level.

5.3 The **Tracking Error** figure is a consolidation of the difference between each Fund Manager's actual return versus their respective benchmark. The unprecedented increase since the middle of 2008 in this measure reflects huge market volatility and the difficult financial market environment facing the Fund (and its investment managers).

5.4 The **Information Ratio** is a measure of manager skill and has been volatile over recent years. The figure has fallen to a negative number which reflects the level of under-performance in the three year period to June 2011 by most Managers, largely due to a poor second half of 2008/09.

6.0 SOLVENCY

6.1 The **solvency position** is presented in **Appendices 3 and 4**. As at 30 June 2011 the estimated solvency had decreased in the last quarter from 70% to 69%. The Solvency position has been updated in **Appendix 3** following the 2010 Valuation hence the large change in solvency between the December 2009 and March 2010 Quarters.

6.2 The assets of the Fund increased by 3% in the Quarter (including new money), whilst liabilities (as modelled by the Actuary), rose by 4.3% hence the 1% reduction in solvency in the Quarter. Yields on long-dated gilts are used as the proxy discount rate to value liabilities, hence lower yields result in higher liability values and vice versa.

6.3 The relative position, over time, between liabilities and assets is shown very clearly in **Appendix 4** which is a simple graph using data from **Appendix 3**. It is clear from this graph that

(a) "liability growth" was matched by "asset growth" for the period March 2004 to March 2007 (hence the steady improvement in solvency from 59% to 67% over that period)

(b) from March 2007 to March 2009 "liability value" accelerated and "asset value" fell which had

(c) a significant and consequential impact on solvency – there is a point where the asset and deficit lines cross - this is effectively the 50% funding point (@ June / September 2008)

(d) during 2009/10 changes in assumptions on inflation and bond yields resulted in no overall change in the valuation of liabilities throughout the year whilst asset values improved strongly over the same period

(e) since April 2010 the improvement in asset values has been achieved alongside a less significant increase in liability values (as modelled by the Actuary), resulting in a small but welcome improvement in solvency

6.4 What this analysis illustrates very clearly is that the Fund has no control over "liability value" because it is effectively generated by market conditions, actuarial assumptions and political decisions. The Fund must therefore concentrate on the performance of its assets.

7.0 SOLVENCY AND LONG TERM HISTORIC CONTRIBUTION RATES

7.1 At the Advisory Panel meeting on 25 May 2011 the outcome of the 2010 Triennial Valuation was discussed, with a particular focus on the solvency level of the Fund in relation to other LGPS Funds and the extent to which this was a consequence of the contribution "holiday" from 1990/91 to 1996/97.

7.2 In brief, the Government revised the funding target for scheduled bodies to 75% for the period 1 April 1990 to 31 March 1993 which gave Funds the opportunity to reduce employer contributions over that period and the subsequent phasing in of contribution increases then required.

7.3 Using investment return reports and other information the Actuary estimated the effect of these reduced contributions on the solvency position as at December 2003, when this issue was last examined. These figures have been extrapolated to the most recent Triennial Valuation, at March 2010.

7.4 At the PFC meeting on 26 May 2011 the solvency position of the Fund in relation to other members of the Society of County Treasurers was graphically illustrated. This graph is reproduced at **Appendix 5** with an additional entry for "NYPF – REVISED" to show the estimated effect had the contribution "holiday" not taken place. The estimated improvement in solvency is 11% from 67% to 78% as at the 2010 Valuation date. The ongoing difference in solvency over the period since the Actuary's calculation in 2003 is further illustrated at **Appendix 6**.

7.5 The conclusion is that the current low level of solvency in comparison to other SCT LGPS Funds is as a direct consequence of decisions made in the early 1990s when the political and economic context of public sector pensions was very different. The focus therefore must be on the current investment strategy and achieving the maximum possible return within acceptable risk parameters. Recent performance in comparison to other LGPS Funds is described in **paragraph 4.4**.

8.0 REBALANCING

8.1 The latest round of rebalancing the Fund's assets took place in July 2011, based on the assets held at the end of the June quarter (see **Appendix 7**). £5m was transferred from Standard Life to cash to address the currency hedging requirement.

9.0 PROXY VOTING

9.1 Available on request is the report from PIRC summarising the proxy voting activity in the period March to June 2011. This report covers the votes cast on behalf of NYPF at all relevant company AGM's in the period and includes an analysis of voting recommendations at selected meetings and responses to company engagement.

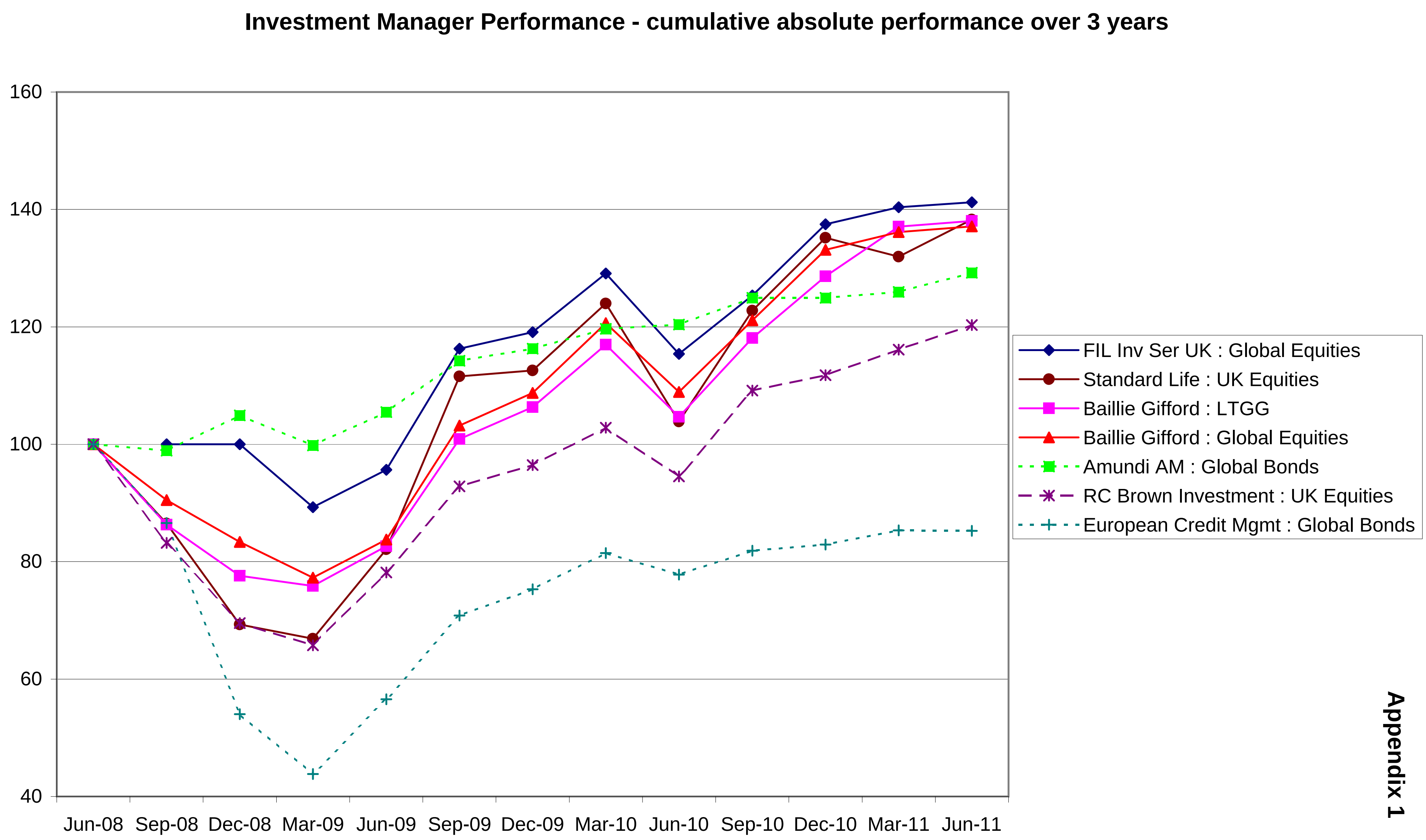
10.0 RECOMMENDATION

10.1 Members are asked to note the investment performance of the Fund for the Quarter and 12 months ending 30 June 2011.

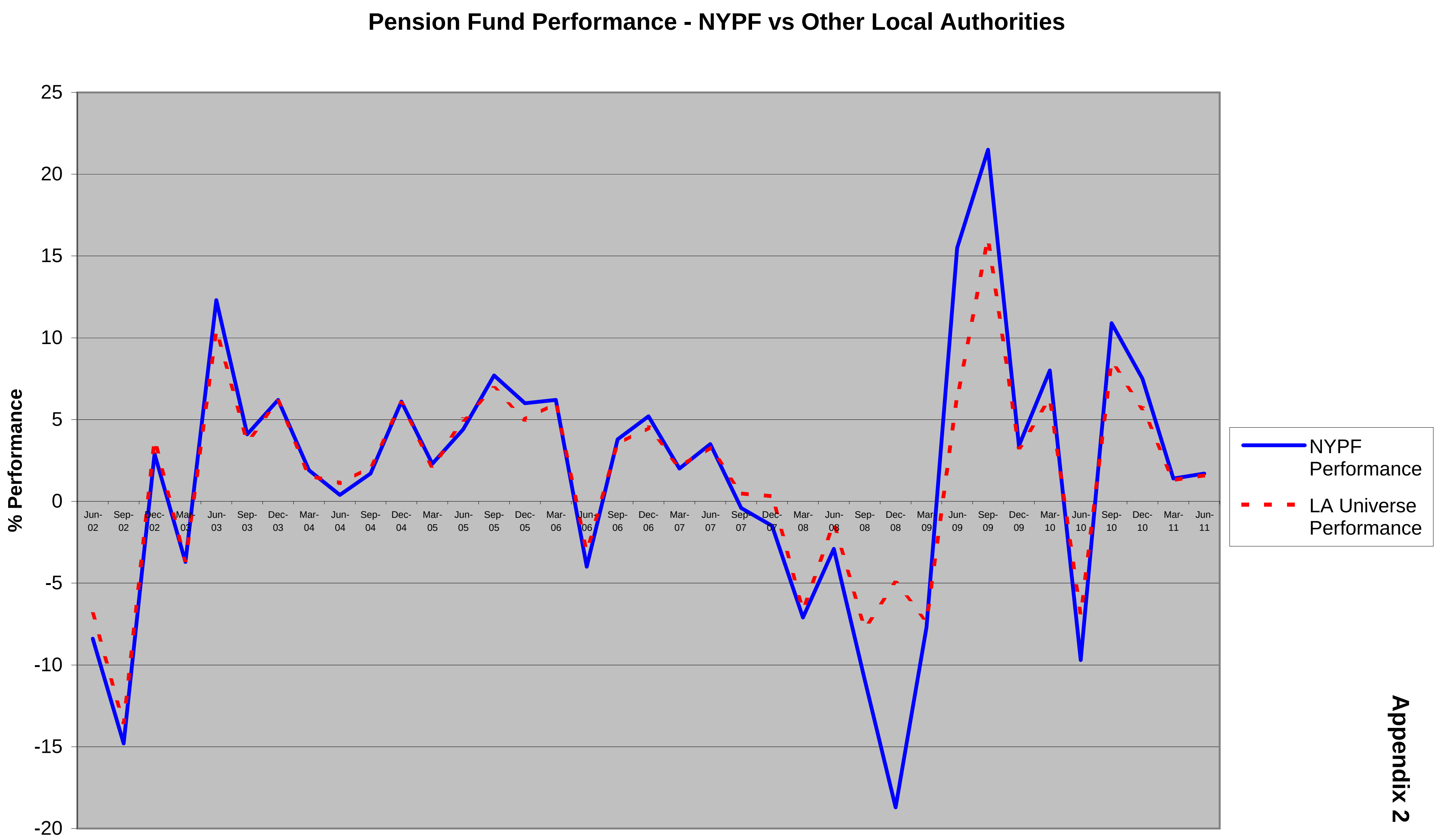
JOHN MOORE
Treasurer, Finance and Central Services
County Hall, Northallerton

14 September 2011

Background documents: None


Investment Manager Performance - cumulative absolute performance over 3 years
160
140
120
100
80
60
40
Jun-08
Sep-08
Dec-08
Mar-09
Jun-09
Sep-09
Dec-09
Mar-10
Jun-10
Sep-10
Dec-10
Mar-11
Jun-11
FIL Inv Ser UK : Global Equities
Standard Life : UK Equities
Baillie Gifford : LTGG
Baillie Gifford : Global Equities
Amundi AM : Global Bonds
RC Brown Investment : UK Equities
European Credit Mgmt : Global Bonds

Appendix 1



Pension Fund Performance - NYPF vs Other Local Authorities
% Performance
25
20
15
10
5
0
-5
-10
-15
-20
Jun-02
Sep-02
Dec-02
Mar-03
Jun-03
Sep-03
Dec-03
Mar-04
Jun-04
Sep-04
Dec-04
Mar-05
Jun-05
Sep-05
Dec-05
Mar-06
Jun-06
Sep-06
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Mar-07
Jun-07
Sep-07
Dec-07
Mar-08
Jun-08
Sep-08
Dec-08
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Jun-09
Sep-09
Dec-09
Mar-10
Jun-10
Sep-10
Dec-10
Mar-11
Jun-11
NYPF Performance
LA Universe Performance

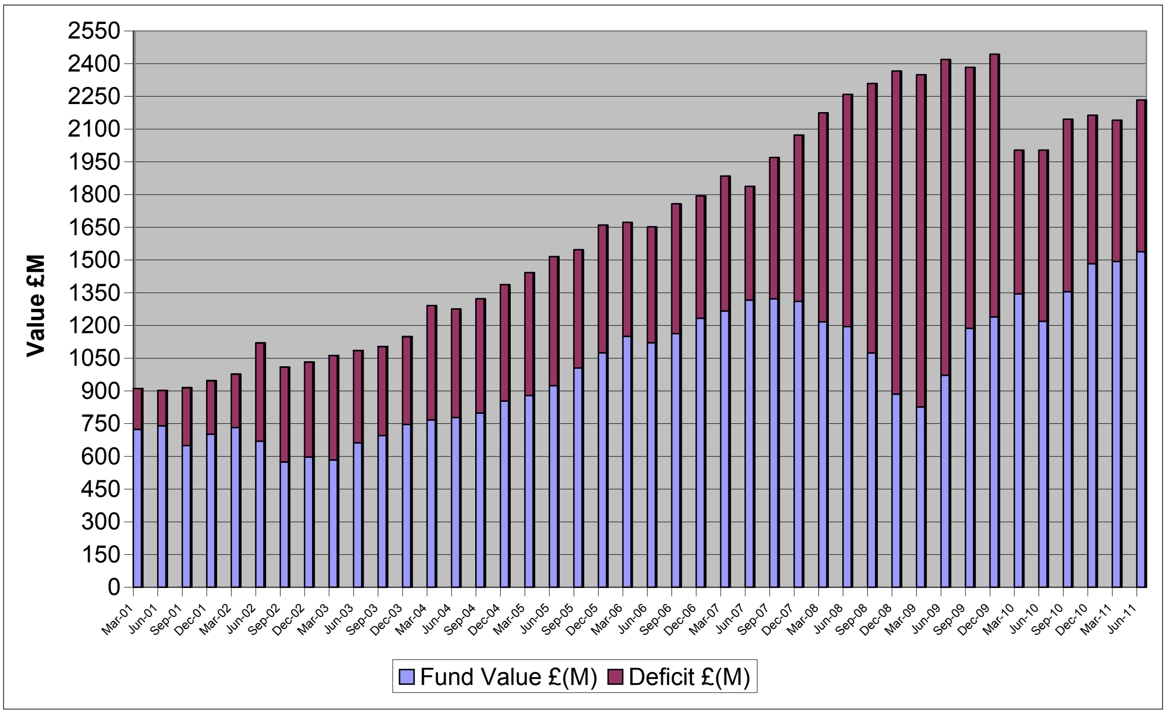
Appendix 2

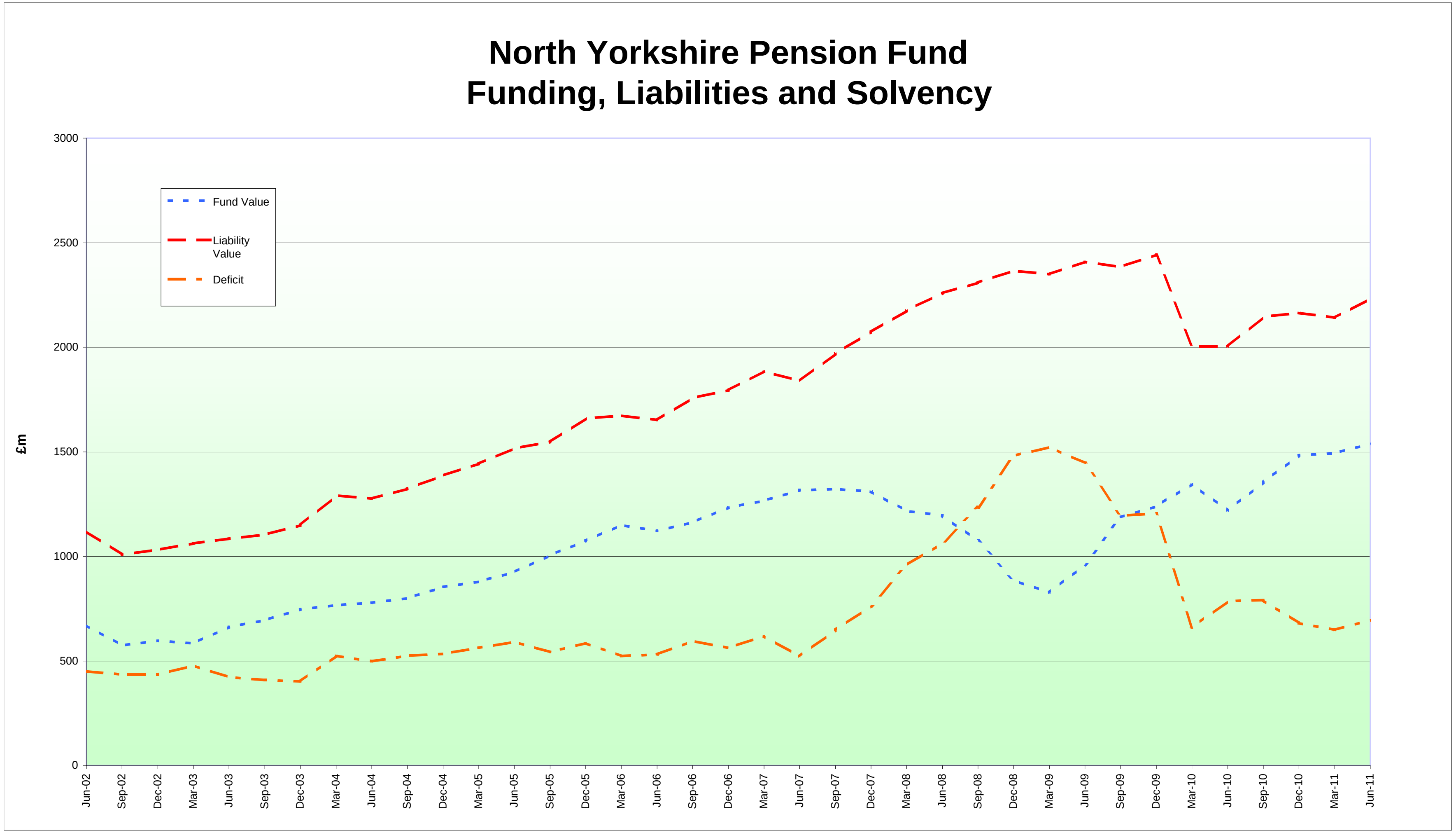
Actuarial Model of Quarterly Solvency Position

Date	Solvency	Deficit £(M)	Fund Value £(M)	FTSE 100
March 31, 2001	79%	187	724	5,634
June 30, 2001	82%	162	740	5,643
September 30, 2001	71%	265	650	4,903
December 31, 2001	74%	245	702	5,217
March 31, 2002	75%	245	732	5,272
June 30, 2002	60%	450	670	4,656
September 30, 2002	56%	435	574	3,722
December 31, 2002	58%	435	597	3,940
March 31, 2003	55%	478	584	3,613
June 30, 2003	61%	423	662	4,031
September 30, 2003	63%	408	695	4,091
December 31, 2003	65%	402	747	4,477
March 31, 2004	59%	524	767	4,386
June 30, 2004	61%	498	778	4,464
September 30, 2004	60%	524	799	4,571
December 31, 2004	62%	533	854	4,814
March 31, 2005	61%	563	879	4,894
June 30, 2005	61%	592	924	5,113
September 30, 2005	65%	542	1005	5,478
December 31, 2005	65%	585	1075	5,619
March 31, 2006	69%	523	1150	5,965
June 30, 2006	68%	531	1121	5,833
September 30, 2006	66%	595	1163	5,961
December 31, 2006	69%	561	1233	6,221
March 31, 2007	67%	619	1266	6,308
June 30, 2007	72%	522	1316	6,608
September 30, 2007	67%	648	1322	6,467
December 31, 2007	63%	763	1310	6,457
March 31, 2008	56%	958	1217	5,702
June 30, 2008	53%	1064	1195	5,625
September 30, 2008	47%	1235	1074	4,902
December 31, 2008	37%	1481	885	4,434
March 31, 2009	35%	1522	827	3,926
June 30, 2009	40%	1447	972	4,249
September 30, 2009	50%	1196	1187	5,134
December 31, 2009	51%	1204	1239	5,413
March 31, 2010	67%	659	1345	5,680
June 30, 2010	61%	785	1219	4,917
September 30, 2010	63%	791	1354	5,549
December 31, 2010	69%	681	1483	5,900
March 31, 2011	70%	648	1493	5,909
June 30, 2011	69%	695	1538	5,946

Triennial valuation results highlighted in grey

Movement in Assets and Liabilities




North Yorkshire Pension Fund
Funding, Liabilities and Solvency
£m
3000
2500
2000
1500
1000
500
0
Fund Value
Liability Value
Deficit
Jun-02
Sep-02
Dec-02
Mar-03
Jun-03
Sep-03
Dec-03
Mar-04
Jun-04
Sep-04
Dec-04
Mar-05
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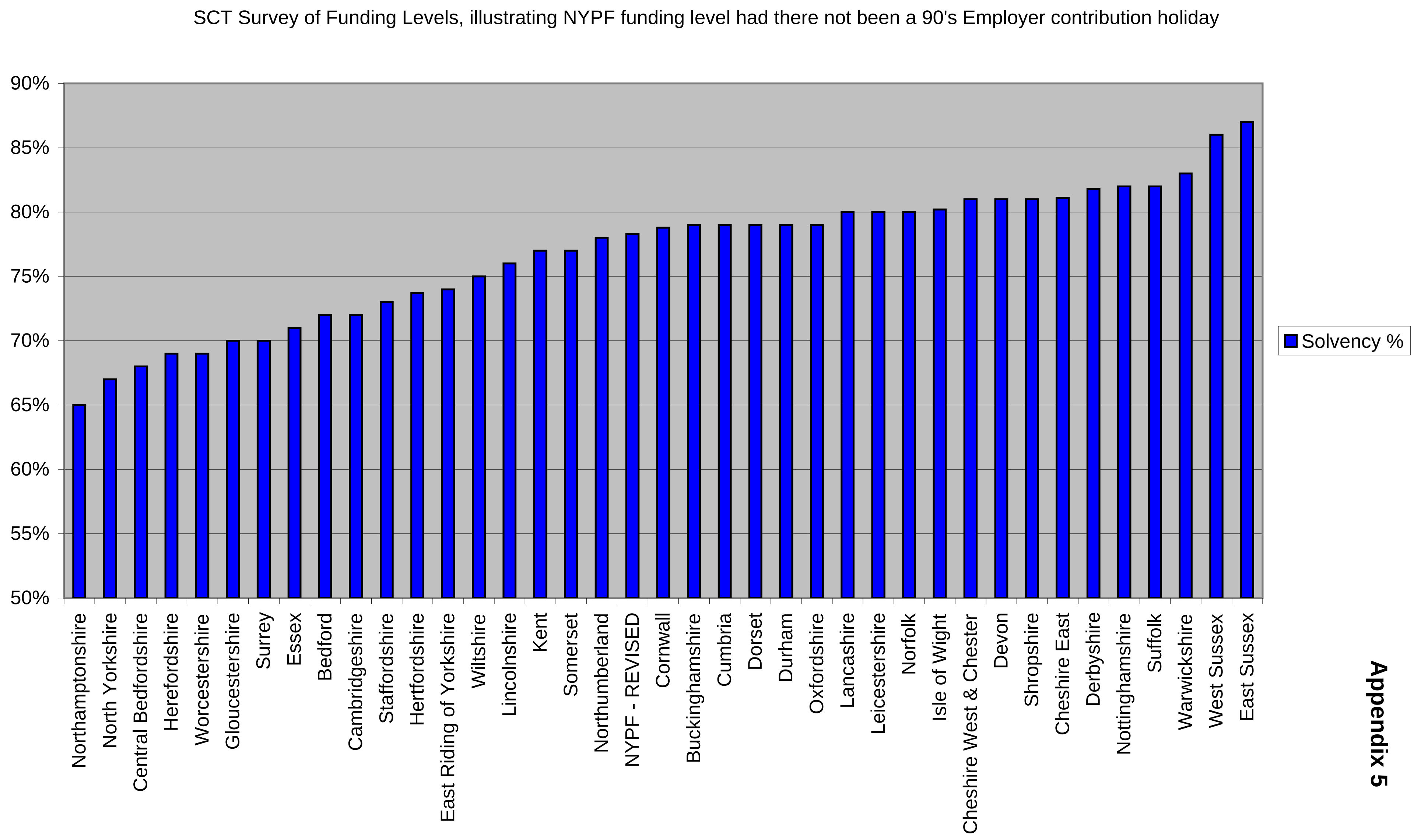
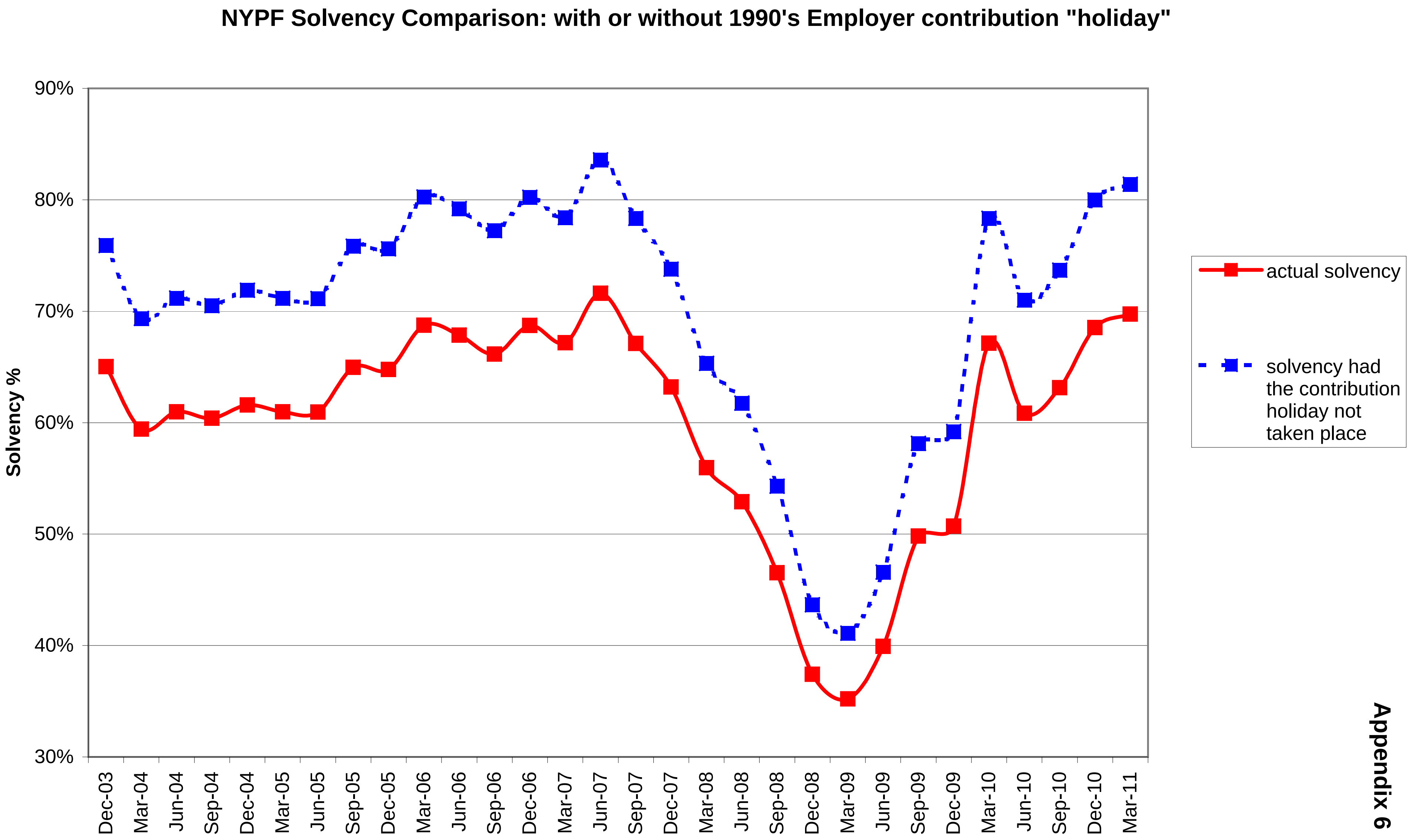
Mar-11
Jun-11

Appendix 4


SCT Survey of Funding Levels, illustrating NYPF funding level had there not been a 90's Employer contribution holiday
90%
85%
80%
75%
70%
65%
60%
55%
50%
Solvency %
Northamptonshire
North Yorkshire
Central Bedfordshire
Herefordshire
Worcestershire
Gloucestershire
Surrey
Essex
Bedford
Cambridgeshire
Staffordshire
Hertfordshire
East Riding of Yorkshire
Wiltshire
Lincolnshire
Kent
Somerset
Northumberland
NYPF - REVISED
Cornwall
Buckinghamshire
Cumbria
Dorset
Durham
Oxfordshire
Lancashire
Leicestershire
Norfolk
Isle of Wight
Cheshire West & Chester
Devon
Shropshire
Cheshire East
Derbyshire
Nottinghamshire
Suffolk
Warwickshire
West Sussex
East Sussex

Appendix 5


NYPF Solvency Comparison: with or without 1990's Employer contribution "holiday"
Solvency %
90%
80%
70%
60%
50%
40%
30%
Dec-03
Mar-04
Jun-04
Sep-04
Dec-04
Mar-05
Jun-05
Sep-05
Dec-05
Mar-06
Jun-06
Sep-06
Dec-06
Mar-07
Jun-07
Sep-07
Dec-07
Mar-08
Jun-08
Sep-08
Dec-08
Mar-09
Jun-09
Sep-09
Dec-09
Mar-10
Jun-10
Sep-10
Dec-10
Mar-11
actual solvency
solvency had the contribution holiday not taken place

Appendix 6

REBALANCING OF NYPF ASSETS AS AT 30 June 2011

Asset Class	Minimum Allocation to Non-Equities	Maximum Allocation to Non-Equities	Current Allocation as at June 2011	Allocation After Rebalancing
Equity + Cash	80%	60%	76.9%	76.9%
Bonds	15%	30%	15.5%	15.5%
Alternatives (ex property)	5%	10%	7.6%	7.6%
Property	0%	0%	0	0
Total	**100%**	**100%**	**100%**	**100%**

		30-Jun-11 Value £m	actual %	**Min %**	**Min £m**	**Max %**	**Max £m**	Under	Over	Rebalancing in July 2011		
Global Equity Managers												
Baillie Gifford Global Alpha		252.94	16.7%	12.0%	182.27	16.0%	243.03	0.00	-9.91	0.00	252.94	16.7%
Baillie Gifford Global Growth		164.65	10.8%	7.8%	118.48	10.4%	157.97	0.00	-6.69	0.00	164.65	10.8%
	(a)	417.59	27.5%	19.8%	300.75	26.4%	400.99	0.00	-16.60	0.00	417.59	27.5%
Global (ex UK) Equity Managers												
Fidelity		368.03	24.2%								368.03	
	(b)	368.03	24.2%	19.8%	300.75	26.4%	400.99	0.00	0.00	0.00	368.03	24.2%
UK Equity Managers												
Standard Life		384.92	25.3%	20.4%	309.86	27.0%	410.11	0.00	0.00	-5.00	379.92	25.0%
Yorkshire Forward		1.34	0.1%	0.0%	0.00	0.2%	3.04	0.00	0.00		1.34	0.1%
	(c)	386.26	25.4%	20.4%	309.86	27.2%	413.15	0.00	0.00	-5.00	381.26	25.1%
Equity sub-total	(a+b+c)=(d)	1171.88	77.2%	60.0%	911.35	80.0%	1215.13	0.00	0.00	-5.00	1166.88	76.8%
Amundi		235.02	15.5%								235.02	
Fixed Income sub-total	(e)	235.02	15.5%	15.0%	227.84	30.0%	455.68	0.00	0.00	0.00	235.02	15.5%
ECM		115.84	7.6%								115.84	
Alternatives sub-total	(f)	115.84	7.6%	5%	75.95	10%	151.89	0.00	0.00	0.00	115.84	7.6%
Cash												
Internal Cash (Barclays a/c)		-0.60								1.00	0.40	
Currency Hedge Cash		-3.22								4.00	0.78	
Cash sub-total	(g)	-3.83	-0.3%	0.0%	0.00	0.0%	0.00	3.83	0.00	5.00	1.17	0.1%
	(d+e+f+g)=(h)	**1518.92**	**100.0%**									**100.0%**
RC Brown	(i)	2.51										
Total Assets	(h+i)=(j)	**1521.43**										

Appendix 7