



MONTHLY UPDATE

Overview

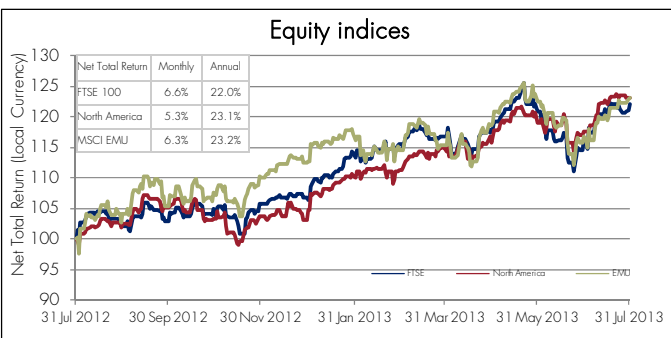
All of the Bank of England's monetary policy members, including new governor Mark Carney, voted against extending the quantitative easing programme beyond its current level of £375 billion, the first unanimous policy decision since October 2012. Both the BoE and the European Central Bank have issued 'soft' forward guidance, saying interest rates are likely to stay low for an extended period of time. This guidance represents a significant change in strategy for the central banks in the way they look to influence the economy.

US investors' concerns over a potential winding down of the Federal Reserve's quantitative easing programme appear to have been appeased. The S&P 500 rose to near record levels last week and was followed by growth in the major stock markets across the globe. The gains in European stocks have led to a rise in UK and German bond yields as demand for safer investments has fallen.

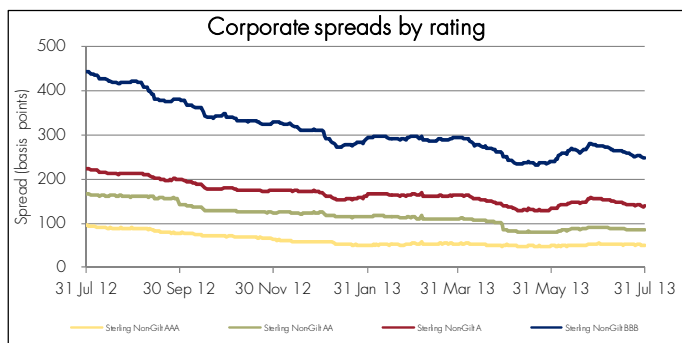
The IMF raised its forecast for growth this year in the UK as evidence of an economic recovery is becoming stronger. The forecast has increased to a 0.9% expansion of the UK economy this year, up from the 0.7% growth forecast in April. Further evidence of the economic recovery was provided as figures showed the UK economy grew by 0.6% in the three months to June.

UK CPI inflation increased from 2.7% in May to 2.9% in June; although this is a 14-month high it was lower than the markets expected. The rise was due to higher petrol and clothing prices.

Equity markets rallied over the month



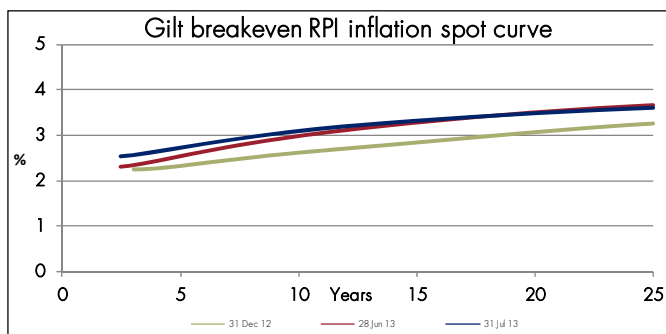
Credit spreads narrowed slightly over the month



LATEST ECONOMIC NUMBERS

Current base rate	0.5%
Quantitative easing level	£375bn
CPI increase June (%y/y)	2.9%
Halifax house prices June (%m/m)	0.6%
IPD TR property index June (%m/m)	0.8%
PPF 7800 funding ratio	89.1%
VIX (volatility) index	13.5
\$/£ exchange rate	1.52
Numbers as at the end of month unless stated	

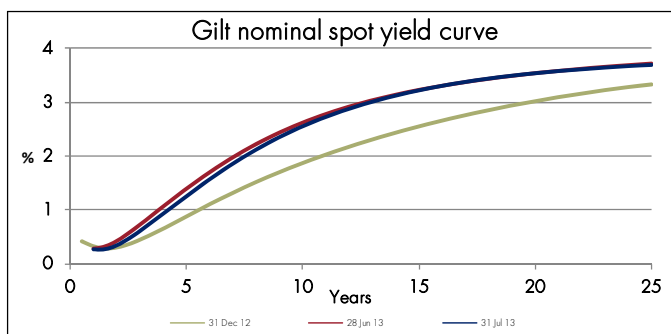
Breakeven inflation increased at shorter durations



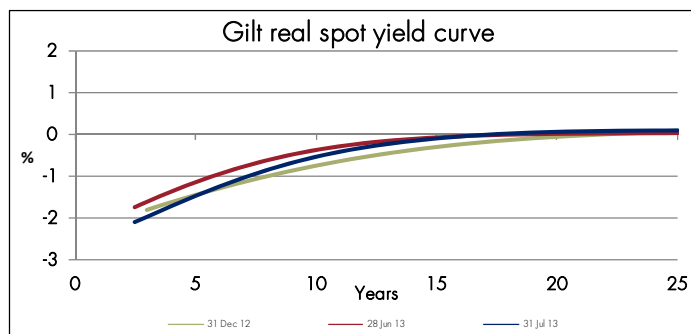
CALENDAR OF EVENTS AND DATA RELEASES

MPC interest rate announcement	1st August
UK Trade	9th August
RPI / CPI	13th August
Minutes of MPC meeting	14th August
Producer Price Index	14th August
UK GDP (Q2 second est.)	23rd August

Nominal yields were broadly unchanged this month



Real yields fell at shorter durations this month





Pension Scheme and Investment Governance

Several recent news stories have brought governance under scrutiny in the pensions industry across Europe. 'Governance' can be used as a broad descriptor covering many aspects of the decision-making process inside a pension scheme. A vital part of a scheme's governance is the controls around the way in which investments are administered and directed by the trustees in fulfilling their fiduciary duties.

What causes poor governance?

The 'Myner's Principles' outline the fundamentals of good governance for institutional investors. They should:

- > Ensure the right people make decisions;
- > Set clear and relevant investment objectives;
- > Be aware and understand risks and their risk tolerance;
- > Arrange a formal process for measuring the performance of both investment managers and trustees;
- > Use or establish policies to discharge responsibilities as an investor including monitoring, voting and if necessary intervention.
- > Keep the members and other stakeholders informed of their actions.

Failure to adhere to these can lead to ineffective governance procedures, for example, poor investment manager selection processes. Poor governance can lead to inefficiencies and potential errors in the decision-making process inside a pension scheme which can lead to sub-optimal outcomes.

There is some evidence that large schemes have better governance procedures than small schemes (see Box 1). It has been suggested this is due to the smaller budgets, both proportionately and in actual spend, that small schemes have to improve their governance. In addition, some commentators have also suggested that there is significant governance risk in relation to DC schemes due to individual member involvement in some key decisions. This includes investment decisions and decumulation decisions, where a lack of knowledge or appropriate delegation can lead to poor decision making.

How can governance be improved?

The Myner's Principles described above were conceived in 2002 and updated in 2008. This month, a poll has indicated more than half of pension schemes are still not satisfied with their current governance structure¹. There are a number of more recent measures to improve pension scheme governance.

The Pensions Regulator has launched several initiatives to improve the level of both defined benefit and defined contribution pension scheme governance. Their primary initiative is the 'Trustee Toolkit', a set of online tools that allows trustees to better understand their responsibilities and improve their knowledge of pension specific issues. The improved understanding should assist trustees in identifying shortcomings in their current governance processes and introducing measures to address these.

Some argue that many of the risks and issues facing smaller defined contribution pensions schemes can be mitigated by the use of master trusts (e.g. NEST) due to the existing governance provided. In addition it allows schemes to benefit from an increased level of governance spending through pooling resources.

Smaller defined benefit pension schemes can overcome a lack of trustee knowledge by placing schemes under a 'fiduciary mandate'. Under such mandates an investment manager will take care of some of the key investment decisions, for example strategic asset allocation, as well as the operational functions. However, in this situation the pension scheme trustees need to take care to properly control any conflict of interests that arise from such solutions and maintain sufficient oversight of the manager's actions and performance.

Does better governance lead to better outcomes?

It is often taken for granted that good governance is more likely to lead to good outcomes. A study has suggested schemes that rated their governance highly had experienced 1-2% higher investment returns². However, many benefits can be difficult to quantify as they offer improvements to human interaction. It is widely considered that good governance is worth pursuing for the softer benefits alone: time saved, greater confidence in decision-making and greater ability to respond to new situations and opportunities. A recent project by Royal Mail, Telnet and Saul to establish a 'Pensions Governance Index' is designed to help pension schemes better understand how to meet their governance ambitions as effectively and efficiently as possible. It is expected to deliver results in Summer 2013.

1. SEI Poll: Majority Of Pension Schemes Feel Current Governance Structures Aren't Working, July 2013.

2. K. Ambachsteer, R. Capelle, H. Lum, 'Pension Fund Governance Today: Strengths, Weaknesses and Opportunities for Improvement' (Financial Analysts Journal, October 2006).

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Contact Information

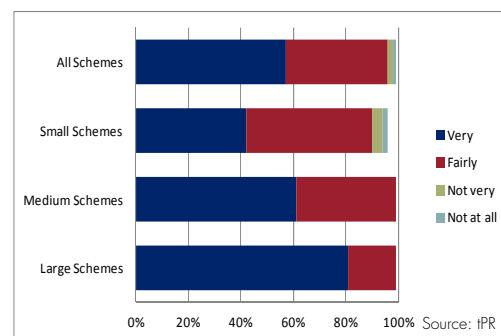
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Box 1 - Overall, how effectively do pension scheme trustees think the trustee board governs the scheme?



This chart shows how governance is considered to be more of an issue for small schemes when compared to larger schemes.