

Disappointing Recent Returns for Pension Funds

Ellen Bailey of Mercer Investment Consulting summarises the performance of Irish pension managed funds since the end of June 2004.

After a strong performance early in the year, equity markets once again stalled as investors focused on a series of concerns including higher oil prices and the prospects of further interest rate hikes. This led to disappointing equity market returns for the quarter to end September with the FTSE World Index down -2.5% over the three months. By contrast, bonds put in a strong third quarter performance with the Merrill Lynch EMU >5 Year Government Bond Index rising by +3.8% during the quarter. This pattern of bond market out-performance continued into the fourth quarter with a similar pattern for October. Overall, the year to date return at the end of October shows the >5 Year Government Bond Index out-performing the World Equity Index by 2.6%.

According to figures released by Mercer Investment Consulting, the average Irish pension managed fund posted a 0% investment return for the third quarter. This is the first quarter not to record a positive managed fund return since the first quarter of 2003 and is likely to be a source of concern for pension funds given the continuing solvency issues that many are dealing with.

PERFORMANCE IN 2004

As at 31st October, AIBIM's Multimanager Managed Fund topped the Mercer survey, returning 7.6% in the year to date compared to an average managed fund return of 5.9%. This was followed by Hibernian Life and Irish Life which jointly tied for second place with a return of 7.3%. This has left the rankings at the top of the table virtually unchanged, highlighting the importance of the relative performances achieved in the stronger equity markets of earlier in the year. The third quarter was disappointing for KBCAM keeping them bottom of the table with a year to date return of 2.5%.

Over the twelve months to end October, ILIM's Managed Fund and Hibernian Life were the best performing funds, achieving +9.2%.

Looking to the future, the current level of outperformance of bonds over equities appears unsustainable to many commentators given the historically low level of bond yields. Most investment managers are predicting equities will outperform bonds over the short to medium term subject to any geopolitical risks that may emerge. This is reflected in the asset allocation that managers have adopted which shows a relatively high level of equity exposure at end September, averaging 72.7% of total assets. This is despite the poor performance posted by equities in the previous quarter.

Around this average of 72.7%, total equity holdings range from 64% to 78%. If there is a significant recovery in equities over bonds in the short term, therefore, the level of equity exposure held by each manager is likely to be a significant factor in explaining differences in fund performances.

Although performance for equities overall was disappointing in quarter three, there were some significant differences in regional and sectoral returns.

The Irish equity market again posted a positive return (3.2%) for the third quarter with managers generally outperforming this benchmark for the quarter. The year to date return to end October is 17.9% making it the best performing equity market over the period. Most managers however failed to achieve the market return year to date.

Elan's strong recovery in value particularly in quarter one (206%), a stock that managers generally held an underweight position in, played a significant role in this underperformance.

Another market that outperformed earlier in the year was the Japanese market, up 15.1% in the first six months of the year. Quarter three saw the Japanese market give up its relative outperformance, down -9.7%, and bring its year to date

(-6.2%). Non-Cyclical Consumer goods was the only other sector to record a negative return over the same period although its performance was only marginally negative (-0.7%).

Despite these broad differentials, volatility at an individual stock level continues to place an emphasis on managers' stock picking skills and this is likely to remain the case for the foreseeable future.

place. This compares to an average return of +1.0%p.a. for the same period. AIBIM and KBCAM tied for last place, both posting -1.7%p.a. over this period.

Again, we need to look to the ten year numbers to get managed fund returns that are more in line with long-term expectations. During this period, the losses suffered over 2000-2002 are overshadowed by the strong growth of the mid to late 1990s and the recent

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returns at end October to 4.0%. This now places that Japanese market below all the other non-Irish regional equity markets over the period with the exception of the US, which returned 2.9% year to end October.

At a sectoral level there were also some notable differences with Resources up 19.5% for the first ten months, benefiting particularly from the Oil price rise and Utilities up 17.5%. IT had a disappointing quarter three, down -11.6%, making it the worst performing sector for the year to end October

LONGER TERM PERFORMANCE

The three year numbers strengthened significantly as quarter three 2001 (in which the average managed fund dropped by -14%), fell out of the numbers. The typical three year managed fund return to end September showed a positive return of +1.6%p.a. compared to the three year end June figure of -3.4%p.a.

Over the five year period to 31st October, Montgomery Oppenheim (+4.7%p.a.) retained poll position, with BIAM (+3.6%p.a.) remaining in second

recovery. The average return for the ten years to end October was +8.8%p.a. The one year average managed fund return of +7.6% to 31st October 2004 compares reasonably well to this and it would be of some reassurance to pension funds if this number could be maintained for 2004.



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GROUP PENSION MANAGED FUND UPDATE AT 31ST OCTOBER 2004

Manager	1 Mth		3 Mths		YTD		12 Mths		3 Yrs		5 Yrs		10 Yrs	
	%	Rank	%	Rank	%	Rank	%	Rank	% p.a.	Rank	% p.a.	Rank	% p.a.	Rank
Acorn Life	0.1	16	1.8	10	5.2	14	6.3	12=	0.4	11=	0.8	8=	9.3	7
AIBIM Managed	0.8	2=	2.3	3	5.3	13	6.3	12=	2.0	14	-1.7	13=	7.7	13
AIBIM Multimanager	0.3	13=	2.0	7	7.6	1								
BIAM Pensions Managed	0.4	10=	1.3	12=	5.4	10=	7.2	10	2.5	1=	3.6	2	10.3	2
Canada Life/Setanta (Series D)	0.8	2=	1.3	12=	6.2	8	9.1	3	0.4	11=	1.4	6	7.9	11=
Davy Exempt Pension Managed	0.3	13=	0.0	16	3.5	15	5.5	14	-0.1	13	-0.2	12	9.2	8
Eagle Star (Balanced)	0.6	4=	2.7	2	6.6	7	8.3	5	1.5	3=	0.8	8=	10.0	4
Friends First / F&C	0.4	10=	1.1	15	5.4	10=	6.6	11	0.7	9=	0.1	11	9.5	5
Hibernian Life	0.6	4=	2.2	4=	7.3	2=	9.2	1=	1.1	6=	1.2	7	9.4	6
Hibernian (NU) Managed	0.6	4=	2.1	6	6.8	5	8.8	4	1.1	6=	1.9	5	10.1	3
Irish Life	0.5	8=	2.2	4=	7.3	2=	9.2	1=	1.5	3=	2.2	4	9.1	9
Irish Life Global Access	0.3	13=	1.9	8=	6.7	6	8.0	6=	1.5	3=				
KBCAM	0.4	10=	1.3	12=	2.5	16	4.3	15	-2.7	15	-1.7	13=	7.9	11=
Montgomery Oppenheim	0.6	4=	1.9	8=	6.0	9	7.8	8	0.9	8	4.7	1		
New Ireland	0.5	8=	1.4	11	5.4	10=	7.4	9	2.5	1=	3.4	3	10.9	1
Standard Life Investments	1.1	1	2.9	1	7.2	4	8.0	6=	0.7	9=	0.2	10	8.3	10
Average	0.5		1.8		5.9		7.6		0.4		1.0		9.3	
Median	0.5		1.9		6.1		7.8		.9		1.0		9.3	