

ITEM NO: 3(a)

GREATER MANCHESTER PENSION FUND ADVISORY PANEL

5 March 2010

Commenced: 10.00am

Terminated: 12.30pm

Present: Councillor Oldham (Chair)

Councillors: Heffernan (Oldham), Mitchell (Trafford), Pantall (Stockport), Pennington (Salford), Smith (Manchester), Walton (Bury).

Employee Representatives

Mr Mulryan, Mr Fraser, Mr Llewelyn, Mr Thompson, Mr Rayner

Apologies for absence: Councillors: Baldwin (Wigan), White (Bolton)

69. DECLARATIONS OF INTEREST

There were no declarations of interest.

70. MINUTES

The Minutes of the proceedings of the meeting of the Pension Fund Advisory Panel held on 20 November 2009 were signed as a correct record.

The Minutes of the proceedings of the meeting of the Pension Fund Management Panel held on 20 November 2009 were signed as a correct record.

71. LOCAL GOVERNMENT (ACCESS TO INFORMATION) ACT 1985

(a) Urgent Items

The Chair announced that there were no urgent items for consideration at this meeting.

(b) Exempt Items

RECOMMENDED

That under Section 100 (A) of the Local Government Act 1972 the public be excluded for the following items of business on the grounds that:

- (i) they involve the likely disclosure of exempt information as defined in the paragraphs of Part 1 of Schedule 12A of the act specified below; and
- (ii) in all circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information for reasons specified below:

<u>Items</u>	<u>Paragraphs</u>	<u>Justification</u>
6, 8, 9, 10, 11 &12	3&10, 3&10, 3&10, 3&10, 1&10, 3&10	Disclosure would or would be likely to prejudice the commercial interests of the Fund and/or its agents, which could in turn affect the interests of the beneficiaries and/or tax payers.

72. ETHICS AND AUDIT WORKING GROUP

The Minutes of the proceedings of the meeting of the Ethics and Audit Working Group held on 22 January 2010 were considered.

With regards to Minute 27, the recovery of withholding taxes on manufactured overseas dividends arising from stocklending, the Head of Pension Fund Investments advised Members of a potential claim against HM Revenue and Customs (HMRC) in respect of withholding taxes suffered on manufactured overseas dividends arising from stocklending.

RECOMMENDED

That the Minutes be received.

73. INFORMATION SERVICES WORKING GROUP

The Minutes of the proceedings of the meeting of the Information Services Working Group held on 22 January 2010 were considered.

RECOMMENDED

That the Minutes be received.

74. LOCAL INITIATIVES AND VENTURE CAPITAL WORKING GROUP

The Minutes of the proceedings of the meeting of the Local Initiatives and Venture Capital Working Group held on 29 January 2010 were considered.

The Chair of the Working Group informed Members with reference to Minute 13 that subsequent to the meeting of the Working Group an investment had been made in the fund in question under delegated powers.

RECOMMENDED

- (i) That the minutes be received; and**
- (ii) With regard to New Initiatives Allocation: PFI and Infrastructure Fund Portfolio, a further report be submitted to a subsequent meeting of this Working Group on a possible increase in the allocation to PFI/Infrastructure funds as part of the review of the Fund's wider investment strategy.**

75. PROPERTY WORKING GROUP

The Minutes of the proceedings of the meeting of the Property Working Group held on 29 January 2010 were considered.

The Chair of the Working Group, Councillor Whitley, informed Members with reference to Minute 13, Greater Manchester Property Venture Fund, planning permission had been granted for the scheme at 1 St Peter's Square (Elisabeth House).

He also made reference to the views expressed by the Advisors at that meeting and at the previous meeting of the Management/Advisory Panel on 20 November 2010, with regard to the Fund increasing its exposure to property generally and specifically the Fund should give consideration to the purchase of agricultural/farmland. As a consequence the Greater Manchester Property Venture Fund (GMPVF) was seeking to increase its landholding in the North West and was in negotiation for the purchase of farmland in Mottram, Tameside and at Davenport Green, Trafford. GMPVF would continue to pursue this policy.

RECOMMENDED

That the Minutes be received, with the addition of B. Thynne to the list of persons present and the removal of C. Lofstedt.

76. VALUATION UPDATE

John Wright of Hymans Robertson, Actuary to the Fund, delivered a presentation which gave an update on the valuation process, current indicative funding position, an explanation of why individual employer results would differ and the scope for stabilising contributions.

He began by explaining that the Fund's assets had grown since March 2007 to February 2010 by approximately 9% but the assessed value of liabilities had increased by considerably more. He added that the funding level of 100% as at March 2007 had fallen to approximately 80% as at the middle of February 2010 if the same basis of determining assumptions was applied. He explained that these numbers were indicative and that they did not reflect the changes to the Fund's membership in the period. He also commented on the basis of the assumptions he had used. The fall in theoretical funding level reflected investment returns being less than assumed and the change in financial conditions and yields. He also commented that he expected GMPF to remain amongst the best funded LGPS funds following the 2010 valuation.

The fall in funding level will necessitate increases in employer contribution rates and indicated the potential scale. The impact will vary significantly at the individual employer level and the Actuary outlined the reasons for this.

In progressing the valuation, traditional tools for stabilising contributions such as the deficit repayment period and phasing in increases or reductions were discussed. This was compared with the approach considered by the Panel in February 2009 of explicit stabilisation rules.

Mr Wright then explained the challenges facing less secure and shorter-term employers. He summarised and outlined the next steps as follows:

- for long term, secure, tax raising employers only, contribution increases be capped at a maximum of 1% per annum for three years;
- the contribution strategy should be tested in terms of prudence, affordability, stabilisation and stewardship;
- the 2010 valuation will be difficult for shorter term and less secure employers and there is a need to consider the available options; and
- further discussion on funding strategy will take place at the next meeting of the Panel.

Mr Wright concluded by stating that the Fund still had better investment returns, a better funding position and lower contribution rates than other Local Government Pension Schemes.

The Executive Director of Pensions advised the Panel of a meeting with employers on 22 April 2010 to discuss in detail the valuation process, the outlook for contributions and the measures that could be put in place to help maintain affordability.

RECOMMENDED

That the content of the presentation be noted.

77. POTENTIAL SCHEME DEVELOPMENTS

Consideration was given to a report of the Executive Director of Pensions and a presentation of the Executive Director of Pensions and the Head of Pension Fund Administration, which outlined potential developments regarding the Scheme and invited the Panel to resolve what the Greater Manchester Pension Fund view should be, and how that view should be promoted.

It was explained that in June 2009 the Department for Communities and Local Government (CLG) published an informal consultation: 'LGPS Delivering Affordability, Viability and Fairness'. This referred to a later exercise that would 'consider new ways in which the LGPS could possibly be reformed to provide more workforce focused pension provision for the 21 Century'. This exercise had not taken place and was not now expected before the General Election.

After the election, the policy themes that CLG may seek to consult on include:

- The LGPS benefit structure and how the costs are met by employees and employers; and
- The scope for achieving economies of scale in fund management structures and benefit administration.

The factors involved in determining the affordability of the Scheme were detailed and the impact of developments elsewhere. For example, the investment returns of the last decade had led to significant deficits, which needed to be recovered.

The Executive Director of Pensions suggested that the starting point for a new scheme were the respective parties first agreeing what was affordable and secondly the level of volatility of cost that was manageable for both the employee and employer. Having agreed the "cost envelope" the next stage was to agree the benefit structure. The Head of Pensions Administration then explained the two extremes of pension scheme design, money purchase (also known as defined contribution) and defined benefit. Within the defined benefit category there were two types of scheme; final salary and pension build-up (also known as career averaging).

The Head of Pension Fund Administration then gave details of the three main benefit structure options for delivering pensions, as follows:

- Money Purchase (or Defined Benefits)
- Final Salary
- Pension Build up (or Career Averaging)

He commented that there were many variations of the above.

The perceived advantages and disadvantages of each of the above were outlined.

With regard to cost reductions that could be applied to defined benefit schemes, he explained the three options to make any pension scheme cheaper from the employers' point of view, as follows:

- Reduce benefits;
- Pay benefits later; or
- Increase employee contributions.

Discussion then ensued with regard to the above, the cost of the Scheme and the viability of different scheme designs.

RECOMMENDED

That work be undertaken in conjunction with Hymans Robertson, Actuary to the Fund on a potential scheme design based on a hybrid option with Pension Build Up (Career Averaging) being the default options and the final salary available to those members who were prepared to pay the extra cost.

78. SUMMARY VALUATION OF THE PENSION FUND INVESTMENT PORTFOLIO AS AT 30 SEPTEMBER 2009 AND 31 DECEMBER 2009

A report of the Executive Director of Pensions was submitted, detailing and comparing the market value of the Fund's investment portfolio as at 30 September 2009 and 31 December 2009.

RECOMMENDED

That the report be noted.

79. UNDERWRITING, STOCKLENDING AND COMMISSION RECAPTURE

The Executive Director of Pensions reported that the Fund accepted sub-underwriting via UBS of one issue in the quarter ended 31 December 2009. It was also reported that Capital International did not participate in underwriting activity. Total underwriting commission received during the quarter was £439,387.

Stocklending income during the quarter was nil and compared with £136,703 in the same quarter of 2008.

Commission 'recaptured' during the quarter was £11,490 and compared with £39,274 in the same quarter of 2008.

RECOMMENDED

That the report be noted.

80. EXTERNAL MANAGERS' PERFORMANCE

The Executive Director of Pensions submitted a report which advised Members of the recent performance of the external Fund Managers.

It was noted that in the quarter to 31 December 2009, Capital outperformed by 1.0% against their benchmark index of 1.5%. UBS had underperformed by 0.5% against their benchmark index of 3.2% and Legal and General had succeeded in tracking their benchmark.

Performance figures for the twelve months to 31 December 2009 were also detailed which showed that Capital had outperformed their benchmark by 1.3%, UBS had also outperformed their benchmark by 2.4% and Legal and General had succeeded in slightly exceeding their benchmark.

The Head of Pension Fund Investments commented on the very good performance of Capital over both the latest quarter and twelve month periods, and of the slightly disappointing performance of UBS over the quarter, but excellent performance over the year.

RECOMMENDED

That the report be noted.

81. REPORTS OF THE MANAGERS

(a) UBS Global Asset Management

John Nestor introduced himself as the Head of the UK division and informed Members that he had been recently appointed.

He handed over to Mr Powers who began by commenting on the market background and reported that equity markets continued to do well. The three and twelve month returns were detailed. He added that the long term performance was very good.

Mr Powers made reference to the measures taken by the Government following the economic downturn, including both the slashing of interest rates and quantitative easing, and added that markets now seemed to be stabilising and economies were beginning to recover.

He stated that following the 'high' of the fiscal stimulus, there was the possibility of a 'low' when the stimulus was withdrawn and public spending was cut following the general election.

It was reported that equities remained attractive in terms of valuation, and the current asset allocation was detailed.

Mr West then reported on the drivers of UK equity performance over the latest quarter and twelve month periods and he reiterated his view that 'Megacaps' offered good relative value going forward.

UK equity positions and sector views as at 31 December 2009 were outlined and discussed.

He concluded as follows:

- A more selective approach to stock selection was likely to pay dividends;
- Economic imbalances haven't gone away;
- Valuation support was relative not absolute;
- Selective pockets of great value persist;
- There is a requirement for a large safety margin plus 'self-help' in order for UBS to hold companies perceived as being 'risky' with the portfolio;
- Positive 'tailwind' anticipated from further narrowing of value dispersion; and
- UBS remained optimistic that they could do well in 2010 with their strengthened team.

The Advisors were then asked to comment.

Mr Moizer congratulated UBS on their performance over the last twelve months. He added that no asset class looked favourable at the moment, and thus agreed with the UBS analysis that valuation support was relative not absolute.

(b) Capital International

Mr Hole began by commenting on the relatively subdued markets over the latest quarter. Results were positive in both equities and bonds with a continued strong recovery in US results.

He reported that since the change in the team, the portfolio had outperformed by 3.3%, including 1.4% from the US.

There was a continued belief that a focus on companies with sustainable growth opportunities in developed markets coupled with high emerging markets exposure was the right stance.

Mr Hole set the quarter four of 2009 in context by contrasting the benchmark return with those of the three previous quarters. He made reference to wild swings in economic outlook and investor confidence which had led to market volatility and significant changes in sector leadership.

Investment results by asset class as at 31 December 2009 were detailed and the asset allocation breakdown for quarter four of 2009 was outlined.

Mr Hole compared the prospective price-earnings ratios of the developed and emerging markets and gave a number of reasons why emerging market fundamentals were stronger, including a more robust fiscal position, greater policy options, healthy banking systems and large foreign exchange reserves.

In summary, Mr Hole explained that the economic outlook in developed markets was for slow growth, with a faster-paced recovery forecast in emerging markets.

Mr Gosztony thanked the Panel for their support. He also explained and reiterated Capital's core values and their investment process.

The Advisors were then asked to comment.

Mr Moizer urged caution with regard to investing in China, highlighting the risk of a bubble in the sector.

Mr Hole, in his response, concurred with Mr Moizer's analysis and stated that two of Capital's analysts were concerned about the threat of inflation in China. However, Mr Hole thought that conditions in China were still satisfactory.

RECOMMENDED

That the reports of the Managers be noted.

82. ADVISOR COMMENTS AND QUESTIONS

Mr Hemingway commented on the scale of the fiscal deficit in some developed markets, including the UK and the possibility of a crisis in Sterling and spike in Gilt yields. However, he noted that whilst the Fund is well positioned for such an eventuality, with approximately one third of assets denominated in overseas currency, and a high percentage of UK company earnings coming from overseas, he thought that there was merit in considering reducing sterling risk at the next meeting of the Panel when investment strategy was the main investment item. He also stated that equities may find it hard to outperform in the face of rising bond yields. He asked the managers to comment on this matter as part of their investment strategy reports. He also thought that there was merit in the Panel considering the case for "absolute return funds" at a future meeting.

Mr Moizer sounded a note of caution regarding the prospect of very slow economic growth for several years to come.

RECOMMENDED

That the comments of the Advisors be noted.

83. PROPERTY INVESTMENT QUARTERLY REPORT

The Head of Property Investments presented his quarterly report on the property investment market together with a summary of recent management and investment activity.

In response to a member's question, the Executive Director of Pensions commented on this Fund's current exposure to property v its benchmark and the case for increasing property exposure. This

matter would be considered at the next meeting of the Property Working Group and Panel as part of the investment strategy report.

RECOMMENDED

That the report be noted.

84. BUSINESS PLAN INTRODUCTION AND PLAN FOR THE YEAR

Consideration was given to a report of the Director of Pensions which outlined the issues facing the Pension Fund and suggested some key tasks for 2010/11 and future years.

It was reported that the key challenge for the future continued to be determining when change was appropriate and when the status quo should be maintained. The risks associated with pension fund investment strategies had been very clearly highlighted in recent years, whereby changes in the value of the Fund's assets did not in the short term at least move in line with the value of its liabilities. This had been illustrated by the decline in funding levels over the last decade, the impact on the costs of the Scheme and the knock on impact on employers. Delivering the 2010 actuarial valuation would be the main task of the year.

He also commented on the actions taken in response to the challenging economic and market conditions, together with progress made on the key tasks identified for 2009/10.

The main drivers of the continued success of the Fund's investment performance were detailed. The potential legislative changes continued to be the main factor in terms of providing administrative services to members and employers, necessitating revisions to systems and procedures, staff and employer training and communication to Scheme members.

He also reiterated the importance of maintaining and developing the day to day service for members and employers.

RECOMMENDED

That the proposed key tasks, as detailed in the report, be approved.

85. LOCAL GOVERNMENT PENSION SCHEME (MISCELLANEOUS) REGULATIONS 2009

Consideration was given to a report of the Executive Director of Pensions which highlighted some of the changes introduced by the above Regulations.

RECOMMENDED

That the content of the report be noted.

86. DRAFT LOCAL GOVERNMENT PENSION SCHEME (MISCELLANEOUS) REGULATIONS 2010

The Executive Director of Pensions submitted a report which noted that the Department for Communities and Local Government (CLG) had issued for consultation proposals to make numerous, mostly minor, amendments to the statutory rules of the pension scheme to correct errors and inconsistencies, improve clarity as well as introducing new provisions.

The Executive Director of Pensions would provide comments to CLG on the proposals on behalf of the Fund.

RECOMMENDED

That the content of the report be noted.

87. GMPF ADMINISTRATION EXPENSES BUDGET 2010/2011

A report of the Executive Director of Pensions was submitted which outlined the 2009/2010 revised estimate and the 2010/2011 original estimate for the Fund's cost of administration. The total budget for investment and administration amounts to 0.12% of asset value. Favourable comparisons were also made with costs at other local authority pension funds.

RECOMMENDED

That the budget for 2010/2011 at £12.9m be approved, together with the development items listed in Table 1 of the report.

88. NEW COMPUTERISED PENSIONS ADMINISTRATION SYSTEM

The Executive Director of Pensions submitted a report which considered the case for and recommended a replacement of the existing computerised administration system. The report outlined details of the existing computerised administration system used in the Pensions Office, which had been in use since 2001.

It was explained that there was a long lead in time for introducing a replacement administrative system and thus it was proposed that the process start in the first quarter of 2010/11. This should allow the replacement hardware and software to go live during quarter one 2011/12.

Accurate costs would not be known until tenders were received, but estimated acquisition and set up costs, which would include the purchase of a new computer, were circa £500,000 to £600,000. Ongoing annual maintenance costs were estimated to be £150,000 compared to existing costs of £130,000 giving a net increase in running costs of £20,000.

It was proposed that an update and more detailed analysis of costs together with a detailed timetable be submitted to the Management Panel or Ethics and Audit Working Group (dependant on time constraints) following initial appraisal of tenders received.

RECOMMENDED

- (i) That the Executive Director of Pensions be authorised to procure a new pensions administration system, subject to a satisfactory tender being received; and**
- (ii) That a further report be submitted to the Ethics and Audit Working Group (or the Management Panel) giving a detailed analysis of costs together with a detailed implementation timetable following initial appraisal of the tenders received.**

89. PENSION FUND LEGAL DEEDS SCANNING PROJECT

The Executive Director of Pensions submitted a report which evaluated the case for and proposed the electronic scanning of existing and new deeds held within the Pension Fund Legal Strongroom including an online hosting service.

RECOMMENDED

That approval be given to invite tenders for the electronic scanning of existing and new documents held within the Pension Fund Legal Strongroom to include an on-line electronic hosting service for a 5 year period.

CHAIR