

ITEM NO: 3(a)

GREATER MANCHESTER PENSION FUND ADVISORY PANEL

11 June 2010

Commenced: 10.00am

Terminated: 12.40pm

Present: Councillor K Quinn (Chair)

Councillors: Baldwin (Wigan), Gartside (Rochdale), Mitchell (Trafford),
Pantall (Stockport), Smith (Manchester), Walton (Bury), White (Bolton)

Employee Representatives

Ms Baines (UNISON), Mr Llewellyn (UNITE) and Mr Mulryan (AMICUS)

Apologies for absence: Councillor Pennington (Salford), Mr Rayner and Mr Thompson

1. DECLARATIONS OF INTEREST

There were no declarations of interest.

2. CHAIR'S INTRODUCTION

The Chair welcomed everyone to the meeting and made reference to the former Chair of the Panel, Councillor S R Oldham. He recognised Councillor Oldham's long service and dedication to the Fund and his contribution towards the many successes of the Fund over his 23 years of leadership.

The Chair extended his congratulations to Mr Bowie, Actuary to the Fund, as the new President of the Institute and Faculty of Actuaries.

3. MINUTES

The Minutes of the proceedings of the meeting of the Pension Fund Advisory Panel held on 5 March 2010 were signed as a correct record.

The Minutes of the proceedings of the meeting of the Pension Fund Management Panel held on 5 March 2010 were signed as a correct record.

4. 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>
7, 8, 9, 10, 11, 12,13 14	3&10, 3&10, 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.

5. APPOINTMENTS

RECOMMENDED

That membership of the Greater Manchester Pension Fund Working Groups for the Municipal Year 2010/11 be as follows:

<u>Working Group</u>	<u>Membership</u>
Ethics and Audit	Councillors: Middleton (Chair), J Smith, Mitchell, Pantall, P Harrison, W Harrison, Sullivan, Messrs: Llewellyn, and Mulryan
Information Services	Councillors: P Harrison (Chair), Beeley, Lane, Middleton, Pantall and Mr Rayner
Local Initiatives and Venture Capital	Councillors: Cooney (Chair), Baldwin, J Smith, Pennington, Ricci, Ms Baines and Mr Mulryan
Property	Councillors: Taylor (Chair), Baldwin, Doubleday, Pennington, J Fitzpatrick, M Smith, Sweeton, Walton, Messrs Mulryan and Thompson

6. ETHICS AND AUDIT WORKING GROUP

The Minutes of the proceedings of the meeting of the Ethics and Audit Working Group held on 16 April 2010 were considered.

RECOMMENDED

- (1) That the Minutes be received.
- (2) With regard to the Statement of Investment Principles:
- (i) That the increase in the limit on 'contributions to partnership' from 5% - 10% be supported;
 - (ii) the changes to the Statement of Investment Principles as required by the regulations be noted; and
 - (iii) the adoption of the revised Statement of Investment Principles be supported.

7. INFORMATION SERVICES WORKING GROUP

The Minutes of the proceedings of the meeting of the Information Services Working Group held on 16 April 2010 were considered.

Councillor Middleton, who had Chaired the Working Group, made reference to the new venue for the Pensioners Forum which was to be held at Lancashire County Cricket Club on 8 October 2010.

RECOMMENDED

That the Minutes be received.

8. 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 23 April 2010 were considered.

RECOMMENDED

- (1) That the Minutes be received.
- (2) With regard to the Specialist Venture Capital (SVC) Strategy Review, that
- (a) the medium term strategic allocation for private equity (SVC and VNW) remains at 4% by value of the total Main Fund assets.
 - (b) the scale of commitment to funds remains at £80m per annum to work towards achievement of the strategy over the next 6 years or so.
 - (c) the Fund continues to implement the revised SVC strategy via 3 year programmes as detailed below:

Geography	Large Buyout	Mid Market Buyout	Venture	Total Number of Funds
EUROPE, inc UK	3 - Direct	6 – Direct	1 - FoF	10
USA	3 – Direct/FoF	3 – Direct/FoF	2 - FoF	8
ASIA		3 FoF		3
				21

Geography	Large Buyout (£m)	Mid Market Buyout (£m)	Venture (£m)	Total (£m)
EUROPE, inc UK	39	76	8	123
USA	36	36	27	99
ASIA		18		240

(d) the target geographical diversification of the SVC portfolio remains as follows:

Europe, inc UK	50% to 55%
USA	40% to 45%
Asia	5% to 10%

(e) the investment stage diversification of the SVC portfolio remains as follows:

Geography	Large Buyout	Mid Market Buyout	Venture
EUROPE, inc UK	30% to 35%	60% to 65%	5% to 10%
USA	35% to 40%	35% to 40%	25% to 30%
ASIA	45% to 50%	45% to 50%	0% to 10%

(f) it continues to be recognised that the portfolio may not fall within the target ranges at (c) and (d) above for a period of 5 – 10 years, because of transitioning from the previous target ranges.

(3) With regard to New Initiatives Allocation: PFI & Infrastructure Fund Portfolio – Strategy report, that:

- (i) The current allocation to PFI/Infrastructure Funds be increased from £120m to a target level of 3% of the Main Fund as part of the Fund’s wider investment strategy; and
- (ii) New fund commitments be phased over a programme period of approximately 4 years, with a target for commitments of between £40m and £80m per annum to between 2 and 4 funds per annum.

9. PROPERTY WORKING GROUP

The Minutes of the proceedings of the Property Working Group held on 23 April 2010 were considered.

RECOMMENDED

(1) That the Minutes be received.

(2) With regard to Property Investment Strategy;

- (i) The long term strategic allocations/constraints remain namely:
 - A strategic allocation of 10% (of Main Fund Value) to property; and
 - The limit on local investment remain at 3%.
- (ii) A broadening of the means by which property exposure was obtained whilst operating with the limits detailed above, as follows:

	Current	Proposed Range
	%	%
In-house Managed (Direct and Indirect)	5	4 - 8
Indirect	1	0 – 2
GMPVF	0	0 – 2
Overseas	0	0 – 2
Other	0	0 – 1
Total	6	6 - 14

- (iii) That a further report be submitted to the next meeting of the Working Group to consider the implementation of the Property Investment strategy approved by the Panel.

10. SUMMARY VALUATION OF THE PENSION FUND INVESTMENT PORTFOLIO AS AT 31 DECEMBER 2009 AND 31 MARCH 2010

A report of the Executive Director of Pensions was submitted, detailing and comparing the market value of the Fund's investment portfolio as at 31 December 2009 and 31 March 2010.

RECOMMENDED

That the report be noted.

11. UNDERWRITING, STOCKLENDING AND COMMISSION RECAPTURE

The Executive Director of Pensions reported that the Fund did not participate in any sub-underwriting via UBS in the quarter ended 31 March 2010. It was also reported that Capital International did not participate in underwriting activity.

Stocklending during the quarter was nil and compared with a charge of £921 in the same quarter of 2009.

Commission recaptured during the quarter was £15,379 and compared with £36,539 in the same quarter of 2009.

RECOMMENDED

That the report be noted.

12. 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 March 2010, Capital had slightly underperformed by 0.1% against their benchmark index of 8.6%. UBS had outperformed by 0.3% against their benchmark index of 6.7% and Legal and General had broadly succeeded in tracking their benchmark.

Performance figures for the twelve months to 31 March 2010 were also detailed which showed that Capital had marginally underperformed their benchmark by 0.2%, UBS had significantly outperformed their benchmark by 6.0% and Legal and General had succeeded in slightly exceeding their benchmark.

The Head of Pension Fund Investments commented on the excellent performance of UBS over the twelve month period.

RECOMMENDED

That the report be noted.

13. ACTUARIAL VALUATION

Consideration was given to a report of the Executive Director of Pensions and a presentation by the Actuary to the Fund, which provided an indication of the expected funding level at the date of the formal triennial actuarial valuation, the reasons for the fall in funding level and the outlook for

employer contributions for the three years commencing 1 April 2011.

The Actuary made reference to the objective of the Fund, which was to provide a low stable employer contribution rate whilst maintaining the solvency of the Fund. He added that over the last three years the Fund had relatively good investment returns, which helped maintain the average rate of employer contributions amongst the lowest of the local authority schemes.

However, it was explained that funding levels had fallen and on an indicative basis, the Fund was currently 81.7% funded as opposed to 99.1% at the last valuation. These indicative results were based on assumptions derived on the same basis as those applied in 2007. More detailed consideration of the assumptions was still required. The indicative numbers do not yet reflect experience of employers. Mr Bowie acknowledged that conditions for the future were expected to be difficult and recognised the potentially challenging outcome of the 2010 valuation. He advised that employer contributions rates for local authority employers (and employers that were pooled with them) were expected to increase incrementally by 1% of payroll per annum over three years.

Issues for less secure employers, and the affordability of higher contribution rates were discussed. These will be difficult and complex issues for the fund and its employers where issues of prudence, stewardship, affordability and stability would need to be considered. The Executive Director also highlighted the demands of managing the valuation process and the resource required.

Discussion also ensued with regard to a rise in interest rates and the effect this would have on the Fund value and employer contributions.

RECOMMENDED

- (1) That the content of the report and the presentation be noted.**
- (2) The formal consultation process for the Funding Strategy Statement be considered by the Ethics and Audit Working Group; and**
- (3) That officers continue to have discussions with employers without a local authority guarantee regarding their scope to provide more security to the Fund.**

14. ACCOUNTING FOR PENSION COSTS – FRS 17

The Executive Director of Pensions submitted a report which set out the fall in funding levels assessed in accordance with the accounting standard FRS 17 that the employers of the Fund may be reporting as at 31 March 2010.

The report summarised that most employers had a very large deficit on an FRS 17 basis of calculation and the scale of deficit had increased materially for most employers, as detailed in the report. However, FRS 17 valuations did not determine the contributions that employers needed to pay into the Fund which were now set until 31 March 2011.

RECOMMENDED

That the report be noted.

15. MAIN FUND AND LONG TERM PERFORMANCE (WM REVIEW 2009)

Consideration was given to a report of the Executive Director of Pensions which advised Members of the excellent long term results for UBS and the Main Fund as a whole, as measured in the WM Annual Review 2009. Detailed results covering periods up to 20 years were given.

The Main Fund was in the top 25% of the Local Authority pension funds surveyed by WM over 3 and 5 years, was in the top 5% over 10 and 15 years and was the best performing Local Authority

fund over the 20 year period.

The long term performance of UBS over their time as a Manager for the Fund had been excellent. However, both UBS and Capital International had underperformed their benchmarks over 3 and 5 years.

RECOMMENDED

That the report be noted.

16. LONG TERM PROPERTY PERFORMANCE (IPD REVIEW 2009 ETC)

The Executive Director of Pensions submitted a report, which advised Members of the recent and longer term investment performance of the Direct Property Portfolio (managed by the internal Property Investments Unit) and of the 'Balanced Property Pooled Vehicle Portfolio' (managed by the Executive Director of Pensions).

Performance in 2009 was 1.0% points above the IPD Universe average and 2.0% points below the Pension Fund average.

Over the three year period, performance was below the IPD average, whilst performance over 5 years matched the IPD average and outperformed over 1, 10 and 20 years.

In considering the whole period of 20 years from the date that the GMPF Management Panel formally set the current performance target of 'median or better', which came into force on the 1 January 1990, the portfolio had beaten the target 11 times and had outperformed the annualised IPD average over the whole period by 0.7% per annum (7.5% per annum versus 6.7% per annum).

The Fund had a strong income base but its income growth projections (at current market rental values) were well below average.

It was reported that the Head of Property Investments would comment on performance and his investment strategy for the 12 months ahead at the Panel meeting in September.

Investments in the Balanced Property Pooled Vehicle Portfolio were also detailed.

It was reported that the enlargement of the property investment portfolio had been achieved in part by investment in indirect property pooled vehicles such as Property Unit Trusts. Some of the indirect property holdings were generalist balanced pooled vehicles which had been selected by the Executive Director of Pensions in order to increase the overall exposure of the Fund to property. The investments held as part of the balanced property pooled vehicle portfolio at the end of March 2010 were detailed in the report together with details of their performance.

RECOMMENDED

That the report be noted.

17. CASH MANAGEMENT

A report was submitted by the Executive Director of Pensions, which explained that the Fund adopted a relatively prudent approach to its cash management. The report outlined the constraints in place to ensure an appropriate level of prudence, focussing primarily on capital preservation and secondly on higher returns. It also detailed the performance achieved last year and over the last three years.

The report concluded that the Pension Fund's cash had been generally well managed. Performance in 2009/10 exceeded market returns and total interest received was £3.4 million.

RECOMMENDED

That the content of the report be noted.

18. REPORTS OF THE MANAGERS

(a) Capital International

Kevin Adams, Fixed Income Portfolio Manager, Capital International, began by reminding Members of the overall objective of the Fund which was maintaining a low, stable employer contribution rate, and also of the investment objective; to achieve a real return of 3.0% to 3.5% per annum.

Capital market assumptions were outlined and the risks to expected returns were detailed as follows:

Reasons why returns may be higher than expected:

- Equities may deserve higher P/E valuation; and
- Economies may be stronger than the cautious base case.

Reasons why returns may be lower than expected:

- Currency volatility rises due to extreme policies;
- Higher than expected inflation;
- Market volatility negatively impacts economic growth;
- Concentration and dividend risks in UK equities; and
- Influence of demographic factors in the longer term.

Mr Adams made reference to demographics and the equity market and summarised Capital's recommendations as follows:

- Consider increasing the allocation to Emerging Markets;
- Continue to move out of UK equity (subject to tactical outlook);
- Implement an allocation to the Global High Income Opportunities Fund; and
- Restructure the bond element of Capital's benchmark.

Martyn Hole, Investment Specialist, Capital International, then focused on Emerging Markets including the growth of Emerging Markets affluence. He also explored the prospect of a 'bubble' in the Emerging Markets but stated that past crises had strengthened their fundamentals. He looked ahead at future investment themes and commented on valuation comparisons between Emerging Markets and the rest of the world. Mr Hole stated that the Emerging Markets were a growing asset class and represented 14.8% of the MSCI All World Index at 31 December 2009 compared to 5% of the Fund's total equities benchmark.

The Advisors were then asked to comment.

Mr Hemingway sought Capital's views on: political risk, transparency of accounting; and environmental risk in Emerging Markets.

Mr Hole explained that the political risk in Emerging Markets (and indeed non-Emerging Markets) was taken very seriously and added that despite its problems, Thailand was one of the best performing markets in the first quarter of 2010. With regard to the transparency of accounting, this had improved substantially over the last couple of years. Capital meet the management of portfolio companies on a regular basis and exercise caution with regard to any conflict of interest. He advised that the impact of global warming was a long term issue, and access to resources, in particular water, were important issues that analysts took into consideration.

Mr Moizer agreed with Capital's general thesis on Emerging Markets and diversification away from the UK. He also commented on the massive growth of Emerging Markets, but highlighted the divide between rich and poor and the possibility of rising tensions.

Mr Hole concurred with Mr Moizer's views with regard to the divide between rich and poor and stated that there was also an issue of a large disparity of income in the West. He added that the Chinese government had started to recognise the huge disparity.

Mr Bowie commented on Capital's outperformance in 2009 and acknowledged their good results.

(b) UBS Global Asset Management

John Nestor, Head of UK, UBS Global Asset Management, commented on UBS' absolute and relative performance in the year to 31 March 2010. He stated that the performance was built on a shared view that risk assets were cheap in March 2009 and that positive contributions had been made by all capabilities and regions.

Current strategic views were summarised as follows:

- Belief that the benchmark remained appropriate for the task;
- Market anomalies were less stark but risk assets like equities continue to offer the best value; and
- Value within equities highlighted by UK megacaps.

David Buckle, Head of Benchmark Relative Return Strategies, UBS Global Asset Management, then explained how the current benchmark helped achieve the Fund's objectives.

He stated that the unprecedented level of government stimulus had aided the global economic recovery but the risk in the financial system had been transferred from corporates to governments and globally, government finances were bound to become stretched. He added that countries without monetary independence were unable to independently devalue their currency, Europe in particular was problematic and the concept of the Economic and Monetary Union was being tested. The benefits for the UK of not being in the Economic and Monetary Union were also outlined.

Mark Powers, Head of UK Value Equities, UBS Global Asset Management, then commented on BP and the Gulf of Mexico incident. He outlined the key issues and financial implications.

The Advisors were then asked to comment.

Mr Moizer congratulated UBS on their outperformance and sought their views on the economy.

Mr Buckle, in his response, stated that he did not think that there would be a 'double dip' recession and made reference to the possibility of another financial asset 'bubble' in two to three years time. He added that the housing market was doing quite well and that borrowing was increasing due to the current low interest rates.

Professor Moizer asked if this affected UBS' allocation to the banking sector.

Mr Powers stated that the Fund was underweight UK listed banks with exposure in the Emerging Markets and overweight UK listed clearing banks. He stressed the importance of a healthy banking sector to the economic recovery.

Mr Hemingway commented on evidence in the United States which would suggest the possibility of a 'double dip' recession. He also expressed concerns regarding sovereign debt.

Mr Buckle explained that inflation was a very real risk that the Bank of England would need to manage carefully.

RECOMMENDED

That the reports of the Managers be noted.

19. INVESTMENT STRATEGY 2010/11

The Executive Director of Pensions submitted a report and gave a presentation that reviewed the benchmark asset allocations for the Main Fund and Fund Managers and considered changes to the investment restrictions.

He stated that the Panel's decision on investment strategy was crucial in determining the investment success of the Fund in relative and absolute terms and that it was key to delivering low stable employer contribution rates. The Fund had a good starting position, having returned to a fully funded position at the 2007 valuation. It also had a track record of good returns and low volatility. The Panel strive to maintain this combination and provided UBS and Capital International with the scope to take tactical positions.

He added that the Fund's relative returns had been driven by the exceptional success of UBS over the five year period from March 2000 to March 2005 and during the last financial year. They now managed just under half the Main Fund assets. This was a high concentration with one manager.

In his presentation, the Director commented on:-

- (i) the investment guidelines within which the Fund's Managers must operate;
- (ii) the required rate of return;
- (iii) historical returns;
- (iv) prospective returns;
- (v) how the Fund investment strategy compares with other funds;
- (vi) a review of the existing investment strategy; and
- (vii) proposed changes to investment strategy.

RECOMMENDED

(1) Any new cash requirements from the securities managers be taken from UBS.

(2) Securities Portfolio – Main fund Asset Allocation

- (a) To maintain the existing strategic asset allocation to Equities 65%:35% Non-Equities. These allocations to be reviewed if the triggers detailed in the report (or as otherwise agreed) are breached.**
- (b) The Equity split be maintained at 50% UK and 50% Overseas.**
- (c) The Overseas Equity split be maintained at : North America 30%; Europe (ex UK) 30%; Japan 17.5%; Pacific 12.5% and Emerging Markets 10%.**

(3) Property

- (a) The long term strategic allocation to property remains at 10% of total Main Fund assets.**
- (b) The limit on local investment (including any non-property local investment) remains at 3% of total Main Fund assets.**
- (c) The benchmark for property be sub-divided to broaden the range of approaches to obtaining the target 10% exposure as follows:**

	Current %	Proposed Range %
In-house Managed (Direct and Indirect)	5	4-8
Indirect	1	0-2
GMPVF	0	0-2
Overseas	0	0-2
Other	0	0-1
Total	6	6-14

(4) Private Equity/Venture Capital

The recommendations of the Local Initiatives and Venture Capital Working Group be adopted (Meeting of the Local Initiatives and Venture Capital Working Group held on 23 April 2010, Minute 20 refers).

(5) Infrastructure

The recommendations of the Local Initiatives and Venture Capital Working Group be adopted (Meeting of the Local Initiatives and Venture Capital Working Group held on 23 April 2010, Minute 21 refers).

(6) Cash

Any requirements for cash in respect of new investment under 3, 4, 5 and in respect of the Special Opportunities Portfolio be taken from the internally managed cash allocation and the relevant benchmark allocation be reduced accordingly.

(7) Special Opportunities

The Panel note the clarification to the 'terms of reference' of the Special Opportunities Portfolio to emphasise that the key requirements are the prospects of delivering increased diversification (away from Fund 'norms'/traditional markets) and good returns – it is not essential that an investment be 'of the moment'.

(8) The Executive Director of Pensions, after consultation with the Advisors where appropriate, determine and advise the Managers of their revised benchmark indices to reflect the decisions of the Panel.

(9) Further Reports

The Management Panel consider further reports covering:

- (i) the appropriate mix between UK and Overseas equity, the sub-division of the Overseas equity allocation and the preferred approach to currency exposure including the possible use of active or passive hedging;**
- (ii) establishing broad based benchmarks for the allocation to bonds;**
- (iii) a review of the active risk limit on the Capital portfolio in the light of benchmark changes actioned in 2008.**

20. ADVISOR COMMENTS AND QUESTIONS

Mr Bowie agreed with the 'steady as you go' approach to the investment strategy recommendations. He commented on plans to 'build up' the property and infrastructure portfolios

and suggested that such moves underscored the need for oversight of these internally managed portfolios by the appropriate Working Groups.

Mr Moizer and Mr Hemingway concurred with the above.

RECOMMENDED

That the comments of the Advisors be noted.

21. PROPERTY INVESTMENTS 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.

RECOMMENDED

That the report be noted.

22. NORTH WEST INVESTMENT FUND (JESSICA)

Consideration was given to a report of the Executive Director of Pensions which informed Members that a consortium had been established comprising Manchester City Council (on behalf of GM authorities, Cumbria, Cheshire and Lancashire), CBRE (an FSA registered Fund Manager) and GMPF (who are providing guidance on investment strategy and as a potential investor), to bid to operate a 'Rest of the Northwest Urban Development Fund'. The report provided background on 'JESSICA' and outlined a potential role for GMPF in benefiting from the deal flow that 'JESSICA' would generate.

RECOMMENDED

- (i) That the Panel support the involvement of the Fund in the consortium bid to be submitted by 18 June 2010; and**
- (ii) That GMPF advise the consortium that up to 25% of the GMPVF allocation (£25m – £50m) could be available to invest in opportunities that meet the Fund's criteria as described in the report.**

23. STATEMENT OF INVESTMENT PRINCIPLES

Consideration was given to a report of the Executive Director of Pensions which advised Members of various changes that were proposed to be made to the Statement of Investment Principles and outlined the reasons for the proposed changes.

RECOMMENDED

That the draft Statement of Investment Principles appended to the report and amended as set out within the report, be approved and adopted by the Fund.

24. GMPF NEWSLETTER

The June 2010 issue of the above was submitted for Members information.

25. DATES OF FUTURE MEETINGS

The dates of future meetings for the 2010/11 municipal year were noted as follows:

10 September 2010 (AGM)
3 December 2010
4 March 2011

CHAIR