# ITEM NO: 3(a)

**GREATER MANCHESTER PENSION FUND ADVISORY PANEL**

**19 June 2009**

**Commenced: 10.00am** **Terminated: 12.45pm**

| | |
|---|---|
| **Present:** | **Councillor Oldham (Chair)** |
| | **Councillors: Baldwin (Wigan), Hobhouse (Rochdale), Smith (Manchester)** |
| | **Employee Representatives** |
| | **Mr Llewellyn (UNITE) and Mr Fraser (GMB)** |
| **Apologies for absence:** | **Councillors: Heffernan (Oldham), Morris (Bolton) and Mr Thompson** |

## 1. DEATH OF COUNCILLOR MARTIN WAREING

The Chair reported with great sadness on the recent death of Councillor Martin Wareing. He paid tribute to his outstanding achievements, both as a Tameside Councillor and as a Trustee of the Greater Manchester Pension Fund. He stated that the death of Councillor Wareing would be a great loss to the Fund and to all who had the pleasure of meeting and working with him.

The Chair requested those present to stand in silence for a few moments, as a mark of respect for the late Councillor Martin Wareing.

## 2. DECLARATIONS OF INTEREST

There were no declarations of interest.

## 3. MINUTES

The Minutes of the proceedings of the meeting of the Pension Fund Advisory Panel held on 6 March 2009 were signed as a correct record.

The Minutes of the proceedings of the meeting of the Pension Fund Management Panel held on 6 March 2009 were signed as a correct record.

The Minutes of the proceedings of the meeting of the Urgent Matters Panel held on 7 April 2009 were signed as a correct record.

The Minutes of the proceedings of the meeting of the Urgent Matters Panel held on 24 April 2009 were signed as a correct record.

## 4. PROJECT GOLF

***At this juncture, Peter Moizer, Advisor to the Fund and a member of the Competition Commission, left the meeting to prevent a conflict of interest.***

The Director of Pensions updated members with regard to an investment opportunity of a confidential nature, details of which had been explained to members at the last meeting of the Panel (Meeting of 6 March 2009, Minute 78 refers).

He explained the current position with regard to the bidding process and abort costs. He also thanked everyone involved in this particularly demanding piece of work, especially Mr Taylor and members of the Investments Team. He added that progress would be reported to the next Panel Meeting.

The Director of Pensions reiterated that Mr Moizer had not participated in any part of the process.

***Peter Moizer rejoined the meeting at this juncture.***

## 5. 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

**RESOLVED**
**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 the circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information for reasons specified below:**

| **Items** | **Paragraphs** | **Justification** |
|---|---|---|
| **5, 9, 10, 11, 12 ,13, 14** | **3&10, 3&10, 3&10, 3&10, 3&10, 3&10, 1&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.** |

## 6. APPOINTMENTS

**RECOMMENDED**
**That membership of the Greater Manchester Pension Fund Working Groups for the Municipal Year 2009/10 be as follows:**

| **Working Group** | **Membership** |
|---|---|
| **Ethics and Audit** | **Councillors: Middleton (Chair), Smith, Mitchell, Pantall, Sidebottom, Harrison, Welsh, Messrs: Llewellyn, McCann and Mulryan** |

| | |
|---|---|
| Information Services | **Councillors: Vacant Post of Chair, Beeley, Heffernan, Hobhouse, Lane, Middleton, Pantall and Mr Rayner** |
| **Local Initiatives and Venture Capital** | **Councillors: Cooney (Chair), Baldwin, Bell, Smith, Hobhouse, Pennington, Ricci, Messrs: Baines, McCann and Mulryan** |
| **Property** | **Councillors: Whitley (Chair), Baldwin, Doubleday, Pennington, K. Quinn, Sweeton, Walton, Messrs McCann, Mulryan and Thompson** |

## 7. ETHICS AND AUDIT WORKING GROUP

The Minutes of the proceedings of the meeting of the Ethics and Audit Working Group held on 17 April 2009 were considered.

**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 24 April 2009 were considered.

**RECOMMENDED**

**(i) That the Minutes be received.**

**(ii) With regard to Project Golf, that the Director of Pensions be given delegated power to approve any bid submission subject to such bid being within the parameters set by the meetings of the Urgent Matters Panel held on 18 February 2009 and 7 April 2009.**

**(iii) In respect of Specialist Venture Capital – Strategy Review, that:**

**(a) The medium term strategic allocation for private equity (SVC and VNW) remained at 4% by value of the total main Fund assets;**

**(b) The scale of commitment to funds remained at £80m pa 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 | Total (£m) |
|---|---|---|---|---|
| EUROPE, inc UK | 39 | 76 | 8 | 123 |

| | | | | |
|---|---|---|---|---|
| **USA** | **36** | **36** | **27** | **99** |
| **ASIA** | | **18** | | **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) 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.**

**(iv) In respect of the New Initiatives Allocation: PFI and Infrastructure Fund Portfolio, that the current allocation to PFI/Infrastructure Funds within the New Initiatives Allocation be increased by £60m, from £60m to £120m, with the allocation 'split' – as under the current strategy – equally between Primary funds (£60m) and Secondary funds (£60m) as part of the Fund's wider investment strategy.**

## 9. PROPERTY WORKING GROUP

The Minutes of the proceedings of the Property Working Group held on 24 April 2009 were considered.

The Chair of the Working Group, Councillor Whitley, explained that with regard to Elisabeth House, it was hoped that planning proposals would be submitted to Manchester City Council in September 2009.

**RECOMMENDED**
**(i) That the Minutes be received.**

**(ii) That with regard to the Property Portfolio, an analysis of current working practices for the processing of payment of rents be completed and the results reported to a future meeting of the Working Group.**

## 10. SUMMARY VALUATION OF THE PENSION FUND INVESTMENT PORTFOLIO AS AT 31 DECEMBER 2008 AND 31 MARCH 2009

A report of the Director of Pensions was submitted, detailing and comparing the market value of the fund's investment portfolio as at 31 December 2008 and 31 March 2009.

**RECOMMENDED**
**That the report be noted.**

## 11. UNDERWRITING, STOCKLENDING AND COMMISSION RECAPTURE

The Director of Pensions reported that the Fund accepted sub-underwriting via UBS of two issues in the quarter ended March 31 2009. It was also reported that Capital International did not participate in underwriting activity. Total underwriting commission received during the quarter was £366,052.

Stocklending income during the quarter was -£921 and compared with £101,183 in the same quarter of 2008.

With effect from 19 September 2008, GMPF temporarily suspended its stocklending programme pending a return to less volatile market conditions.

Commission 'recaptured' during the quarter was £36,539 and compared with £24,053 in the same quarter of 2008.

**RECOMMENDED**
**That the report be noted.**

## 12. EXTERNAL MANAGERS' PERFORMANCE

The 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 2009, Capital outperformed by 1.1% against their benchmark index of -8.3%. UBS had underperformed by 1.7% against their benchmark index of -7.8% and Legal and General had succeeded in broadly tracking their benchmark.

Performance figures for the twelve months to 31 March 2009 were also detailed which showed that Capital had underperformed their benchmark by 1.4%, UBS had underperformed their benchmark by 0.4% and Legal and General had succeeded in tracking their benchmark.

**RECOMMENDED**
**That the report be noted.**

## 13. MAIN FUND AND LONG TERM PERFORMANCE

Consideration was given to a report of the 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 2008. 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 all medium and long-term standard time periods and was the second 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.

Discussion ensued with regard to the current position of the Fund.

**RECOMMENDED**
**That the report be noted.**

## 14. LONG TERM PROPERTY PERFORMANCE (IPD REVIEW 2008 ETC)

The 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 Director of Pensions).

It was a very difficult year for commercial property with values falling by over 25%. The GMPF total return in 2008 was -21.3%, approximately 1% above the IPD Universe average. The direct held properties had delivered a return of –18.4% but the specialist pooled vehicles had had an adverse effect with a return of –29.9%.

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

In considering the whole period of 19 years from the date that the GMPF Management Panel formally set the current performance target of 'median or better' performance, which came into force on the1 January 1990, the portfolio had beaten the target 11 times and had outperformed the annualised IPD average over the whole period by 0.7% pa (7.7% pa versus 6.9% pa).

The Fund has 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 over the past 7 or 8 years 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 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 2009 were detailed in the report together with details of their performance.

**RECOMMENDED**
**That the report be noted.**

## 15. REPORTS OF THE MANAGERS

### (a) Capital International

Mr Brett began by commenting on the Fund's investment strategy. He considered the long term outlook and explained that it was difficult to forecast long term. However, he thought that the current long term strategy would meet the long term objectives of the Fund.

Capital market assumptions over a 10 year horizon were given and the risk-return profile of the current benchmark and a theoretical alternative allocation were outlined.

Mr Brett also stated that sentiment in the corporate bond market was improving, however he urged caution with regard to the outlook for equities.

Risks to the expected returns for the various asset classes were detailed and discussed.

Capital's recommendations were summarised as follows:

- Consider an allocation to Global High Income Opportunities Fund;
- Consider increasing the Main Fund strategic allocation to Emerging Markets Equities from current levels;
- Consider reducing the overall equity allocation in favour of UK Corporate bonds; and
- Spend down cash.

Mr Hole then commented that it had been a better quarter for portfolio returns, and although the long term performance was poor, this was the second successive quarter of outperformance by Capital.

He went on to detail the equity regional breakdown and added that following the replacement of a portfolio manager, there had been better results in North America.

The regional breakdown of fixed income and the equity sector breakdown were also discussed.

With regard to the economic outlook, Capital held a cautious view on medium and long term growth. The effect of three coinciding cycles was also explored. Mr Hole explained that the inventory cycle could be very painful this time and that the outlook for capital spending was poor, but households had increased spending.

Mr Hole summarised that the financial crisis would lead to lower trend growth due to the following factors:

- Lower investment rates as cost of capital rose;
- Banks more cautious to lend;
- Public sector crowds out private investment;
- Persistent increase in unemployment; and
- Impact of lower net worth on consumer habits.

The Advisors were then asked to comment.

Mr Hemingway asked Capital for their views on the outlook for active fund managers and whether the credit crunch was over in terms of bank bailouts.

Mr Hole stated that the outlook for active managers over the next seven years was good. He referred to IMF forecasts for UK bank bailouts that were still required, and stated that we would see further capital raisings by a variety of means.

Mr Moizer made reference to Capital's recommendation to reduce overall equity allocation in favour of UK corporate bonds, stating that not all fund managers would be making this recommendation. He also made reference to Capital's volatility assumptions, questioned why Capital were negative on the utilities sector and noted that Capital were generally taking stock, not sector positions.

Mr Hole agreed that Capital were not taking significant sector positions but that within sectors they were taking big positions, for example, within the financial sector. He explained that Capital were negative on the utilities sector as it was deemed to be expensive, amongst the worst in terms of leverage and was exposed to regulatory risk.

**(b) UBS Global Asset Management**

Mr Harrison began by commenting on UBS's poor performance in the last quarter relative to the benchmark and informed members that the portfolio was now positioned for recovery. He added that there were better signs in the economy and that the fiscal stimulus was starting to show results.

It was reported that financial markets were becoming more stable and that equity markets looked more attractive.

Mr Powers commented on the Fund's current asset allocation, proposed some changes intended to mitigate inflation risk, and outlined the four key themes of UBS' 2009 strategy.

He added that equities were cheap, he was confident that UBS would outperform in stock selection going forward and that UBS had selected stocks with high betas so that as the market rises, so too would the portfolio.

The Advisors were then asked to comment.

Mr Bowie asked UBS to explain changes in the Fixed Income team.

Mr Harrison, in his response, explained that the bond portfolio had underperformed last year and a view had been taken earlier in the year that the UK and Global fixed income teams should be integrated. He outlined changes in the UK team and added that the markets had improved since March 2009.

Mr Moizer commented that the equity selection seemed right, that he understood the beta concept, and that UBS were still light on mining companies.

Mr Powers responded that when taking a long term view on metal prices and the supply and demand picture, the mining sector does not represent good value.

## 16. INVESTMENT STRATEGY

The 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. 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 69%:31% Non-Equities. These allocations to be reviewed if the triggers detailed in the report 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%.**

**(d) The corporate bond allocations be increased from 20% (of non-equity allocation) to 30% by reducing the government bond allocation and cash holdings.**

**(e) The index linked gilt allocation be increased from 8% (of non-equity allocation) to 14% by reducing the government bond allocation and cash holdings.**

**(3) Property**

**(a) The long term strategic allocation remains at 10% of total Main Fund assets.**

**(b) A net budget of £50m be approved for opportunistic property investments up to a maximum of £50m through the in-house manager and GMPVF.**

**(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 24 April 2009, Minute 22 refers).**

**(5) Infrastructure**
**The infrastructure allocation be increased from £60m to £120m in line with the recommendation of the LI&VC Working Group (Meeting of the Local Initiatives and Venture Capital Working Group held on 24 April 2009, Minute 23 refers).**

**(6) Cash**

**The benchmark allocation to cash be reduced to 1% of Main Fund value to enable implementation of the investment changes recommended in this report (such changes to be phased in line with new investments).**

**(7) The Director of Pensions, after appropriate consultation with the Advisors and Managers and Chair of the Panel determine the timing and phasing of the implementation of the decisions of the Panel.**

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

**(9) Further Reports**

**The Management Panel consider further reports on:**

**(i) reviewing the active risk limit on the Capital portfolio because of recent benchmark changes.**
**(ii) proposals made by the Fund's managers and advisors.**

**17. INVESTMENT MANAGEMENT ARRANGEMENTS**

David Cullinan of WM attended the meeting and gave a presentation with regard to the changing structure of Local Authority funds over the last 10 years. The purpose of the presentation was to inform the debate on the merits of alternative investment management arrangements.

The following issues were explored and discussed:

- Risk/Return 2003 – 2005 and 2006 - 2008;
- Analysis of costs;
- Influence of alternative investments;
- Influence of currency hedging; and
- Structures and Asset strategy.

He concluded by explaining that funds were becoming more complex, that structure and asset mix influence short term performance, but it was the investment benchmark that counted most in the long term.

Discussion ensued with regard to the current position of the Fund and its own investment management arrangements. There was no compelling evidence that any alternative approach would be more likely to lead to better outcomes going forward.

## 18. 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.**

## 19. LIABILITY OF FORMER SCHEME EMPLOYERS – IMPLICATIONS OF THE SOUTH TYNESIDE CASE

Consideration was given to a report of the Director of Pensions which outlined and commented on the Court of Appeal's judgment in a recent case involving responsibility for funding deficits relating to scheme employers ceasing to participate in an LGPS fund.

The report detailed the outcome and implications of the judicial review proceedings which ended in December 2007 and the Court of Appeal decision in April 2009.

In conclusion, it was reported that the position in relation to the liabilities of departing scheme employers had been clearly stated by the Court of Appeal, and bearing in mind the judges' comments about the need for legislators to determine matters of financial policy, the onus was on the Department for Communities and Local Government to consider whether regulatory changes were required to change the position to protect the interests of remaining employers and to consult interested parties on their proposals.

**RECOMMENDED**
**That the Director of Pensions be authorised to make representations to DCLG suggesting appropriate scheme amendments.**

## 20. THE LGPS (AMENDMENT) REGS 2009 (SI 2009/1025)

The Director of Pensions submitted a report which commented on recent amendments to the Scheme that paved the way for cost sharing.

**RECOMMENDATIONS**
**That the report be noted.**

## 21. THE REGISTERED PENSION SCHEMES (AUTHORISED PAYMENTS) REGS 2009 (SI 2009/1171

A report was submitted by the Director of Pensions which commented on two aspects of the above regulations: the commutation of small pensions and overpayments of pension upon death.

**RECOMMENDED**
**(i) That the developments regarding commutations be noted;**
**(ii) That the restoration of the waiving of overpayments in the month of death, for those that die before pay day, be approved.**

## 22. ACCOUNTING FOR PENSION COSTS – FRS 17

Consideration was given to a report of the Director of Pensions which outlined a reduction in employers' funding levels on an FRS basis between 31 March 2008 and 31 March 2009.

However, it was also noted that FRS valuations do not determine the contributions that employers need to pay into the Fund. These contribution rates are set until 31st March 2011.

**RECOMMENDED**
**That the report be noted.**

## 23. GMPF QUARTERLY NEWSLETTER

Issue 31 of the above was submitted for Members information.

## 24. DATES OF FUTURE MEETINGS

The dates of future meetings for the 2009/10 municipal year were noted as follows:

18 September 2009
20 November 2009
5 March 2010

**CHAIR**