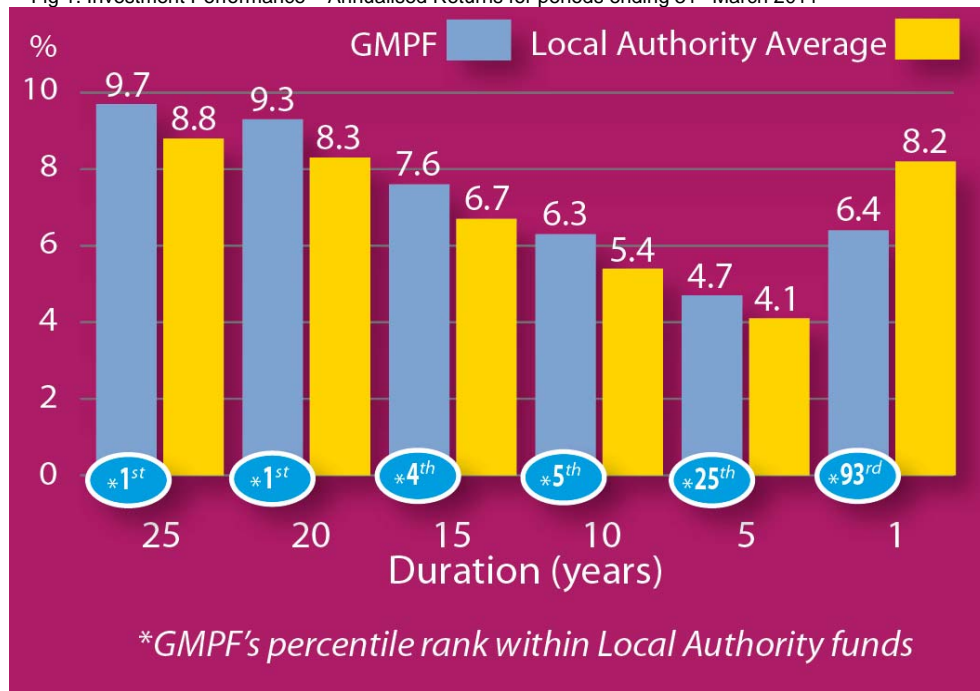


GREATER MANCHESTER PENSION FUND – BACKGROUND PAPER FOR DISCUSSION WITH BOB NEILL

1. BACKGROUND TO GREATER MANCHESTER PENSION FUND

Key Statistics	
1.	Employers – 10 local authorities of Greater Manchester and 250 other employers.
2.	Members – 267,000
3.	Assets - £11bn as at 31 st March 2011
4.	GMPF is approximately 7% of the LGPS, this is bigger than all of the Welsh Funds combined.
5	At 96.4% GMPF's funding level was ranked second in the CIPFA Survey of 2010 valuation results.

Fig 1. Investment Performance – Annualised Returns for periods ending 31st March 2011



1.1 A 1% investment return is likely to equate to all employee contributions due this year (2011/12).

Fig 2. Comparison of GMPF Actual Value v Value based on average LGPS return



1.2 The additional return from GMPF investment returns v the local authority average since 1987 is approaching £2bn.

1.3 Unit costs 2010/11 (source DCLG SF3 Results) – see table below:

Cost per Member			
	Administration £	Investment £	Total £
GMPF	14.07	41.37	55.44
Met Funds	23.05	38.91	61.96
All authority	30.18	76.89	107.07

1.4 GMPF's unit costs for administration are second lowest amongst administering authorities responding to the CIPFA 2010/11 benchmarking service. Using DCLG results GMPF is saving over £2m per annum on its administrative costs compared to the met fund average.

2. WHY HAD GMPF BEEN SUCCESSFUL?

2.1 Stability of Arrangements - Since Tameside became the administering authority in 1987, the Fund has adopted an inclusive approach to its decision making. All the local authorities of Greater Manchester have been represented on the decision making committees together with 6 representatives of the trade unions. This approach is particularly helpful when matters are not going well in that Panel members can explain within their own organisations the rationale behind the Fund's approach and this helps ensure decisions are taken with a long term perspective. Meetings are also held with Treasurers and representatives of employers on a regular basis, quarterly for local authorities and half yearly for other employers. There has been stability and consistency in Panel membership enabling

experience and judgement to develop over time and lessons learnt. Similarly there has been continuity in the Fund's investment management arrangements, key service providers, external advisors and officer support.

2.2 Constancy of Purpose - Throughout its history, the Fund's aim has been: "To deliver low, stable employer contribution rates whilst maintaining the solvency of the Fund." The Management Panel recognises the need for balance in its decision making and the need to manage contradictory objectives. Its success is illustrated in the 2010 Valuation Surveys that rank GMPF in the top 3 funds in terms of its strength of funding with employer contributions at the lower end of the range.

2.3 Economies of Scale - The benefits of economies of scale come through in lower unit costs. There is also the scope to develop internal specialisms to help with both administrative and investment matters. Using our administrative unit costs as an example our advantages include:

- (i) productivity gains/scope for specialisation;
- (ii) relatively stable workforce;
- (iii) relatively low cost area.

The scale of the Fund also makes it easier to buy in services at a competitive price and to buy in external help and advice where the service cannot be delivered effectively or efficiently internally. The Fund has also adopted policies that help improve efficiency and economy.

3. LOCAL INVESTMENT AND SUPPORTING ECONOMIC GROWTH

Part A - GMPF Activity

3.1 The Fund has been investing locally for over 20 years on a relatively small scale. It has always been clear that such investment should satisfy the twin aims of:

- (i) commercial returns;
- (ii) helping the area.

3.2 So far, the most successful form of local investment has been through Greater Manchester Property Venture Fund. As its name suggests, it targets property investment in the North West with a focus on Greater Manchester. The investment is normally development or redevelopment activity. The funding problems being experienced by the banks and the risk averse approach of developers outside London is starting to generate a number of opportunities for the Fund. **The speed of investment in development opportunities would increase if it were possible for the Government to provide more assistance with marginal schemes.** The Fund is working with local authorities to facilitate development in the North West focussing on Greater Manchester. In the current environment, the Fund is becoming one of the most active developers in the North West

3.3 The lack of investment by the private and public sectors may create investment opportunities for the Fund in a number of new areas. As first steps, to try and capture these wider opportunities:

- (i) the Panel has approved an increased allocation of 5% to local investment;
- (ii) created a Business Development Working Group to oversee the identification and thorough appraisal of opportunities, together with evaluating whether appropriate mechanisms are available and can be established to capture the investment opportunity.

- 3.4 Possible further areas for local investment being investigated include:
- (i) housing development;
 - (ii) lending to developers;
 - (iii) low carbon and infrastructure opportunities
 - (iv) invest to save opportunities in the public sector, e.g. social care, reducing crime.
- 3.5 Many of these potential investments will require innovative solutions, including partnerships and joint ventures with public and private sector organisations. If successful, there may be scope for other funds to adopt a similar approach. The key elements of a successful investment are to identify opportunities and delivery mechanisms that can offer commercial returns. **It would be good if DCLG could help in the delivery of some pilot projects.**

Part B - Supporting Local Economic Growth

- 3.6 A recent 'New Local Government Network' (NLGN) article posed the question: "Can local government pension funds fill the infrastructure finance gap?". The article highlights a more detailed NLGN report ("Capital Momentum").
- 3.7 Reductions in Government and Local Government spending sit alongside significant need for new infrastructure to help rebalance the economy and maintain international competitiveness. Infrastructure investment can be an attractive asset class for pension funds, combining long term inflation linked returns with a risk profile at the more prudent end of the spectrum. Local authorities are at the heart of dealing with a locality's economic challenges. It is natural, therefore, that local authority pension funds, such as GMPF (subject always to the overriding need to fulfil the fund's fiduciary duties), will have a great interest in exploring ways in which their objectives as a pension fund can be meshed with the needs of the locality to the benefit of all parties. Potentially therefore, the LGPS is a significant source of potential investment finance.
- 3.8 NLGN identify the challenge of finding a mechanism that can bring the interests of the locality/local authority and the pension fund together, and suggest two key requirements as being necessary to facilitate this.
- 3.9 Firstly, there is a need for the geography and scale of investment to match the needs of the pension fund and the local authorities concerned, and this is likely to require a degree of aggregation or pooling of infrastructure and regeneration schemes. It would be difficult to mobilise pension fund investment for the scale of requirement of any particular individual local authority capital programme. Secondly the types of projects involved must be suitable for both pension funds (in particular with regards to risk/return profile) and local authorities (in terms of meeting local needs).
- 3.10 This situation requires dialogue between local authorities and pension funds to explore different ways of fulfilling the two key requirements and rising to the challenge. **It would be good if DCLG could assist in promoting such dialogue.**

4. CHANGES IN MEMBERSHIP – POTENTIAL PERFECT STORM?

4.1 Analysis of Membership Changes since 31 March 2008

	March 2008	March 2009	March 2010	March 2011	Oct 2011
Employees	103,330	101,913	101,860	97,014	90,995
Deferreds	69,740	76,113	80,195	85,628	88,267
Pensioners	76,110	78,464	80,876	84,673	87,941
Total	249,180	256,490	262,931	267,315	267,203

4.2 By the end of the financial year, employees will be the Fund's smallest category of member!

4.3 Analysis of Recent Numbers of Members Opting Out of the Scheme – see table below

	2009	2010	2011 *
Q1	184	290	309
Q2	189	236	205
Q3	224	298	227
Q4	176	386	
Total	773	1210	741

(*Dependant on employers forwarding data).

4.4 As expected, there has been a big increase in the number of members retiring or taking severance/redundancy and resolving these cases has been a priority for employers. Thus there are potential backlogs of work, e.g. re advising the administering authority re opt outs. In 2010, the opt out rate had increased to around 1.25% of membership. In 2011, this appears to have reduced slightly albeit with the caveat highlighted above.

4.5 Fund concerns re falling employee membership - The environment in which the Pension Fund is operating is changing materially and this will have a big impact on dealing with/managing employer issues that will arise in the future:

- (i) at the individual employer level, there is a wide range of maturity profiles and employer specific funding levels;
- (ii) the proportion of pensioner and deferred members is increasing rapidly at many employers as they shrink their workforce;
- (iii) the risk of employer failure is growing;
- (iv) the changes in membership will have cash flow implications and lead to increased volatility of cost;
- (v) the investment implications of managing this change is likely in the long term to result in higher costs;

- (vi) there will be an adverse impact on society and the public finances of employees not saving for their retirement; and
 - (vii) the impact on membership at the individual employer level of policy changes (e.g. academies) is adding to the problem of increasing maturity.
- 4.6 At the overall fund level, the issues are becoming more complex, but where an employer has net negative cash flow and a low funding level, this is a particularly bad combination for the employer. It is also a serious concern for the guarantor and / or the administering authority.
- 4.7 What is GMPF doing to help address the potential issues?
- Created an employer team – but expertise needs to be developed
 - Appointed the Actuary to undertake some case studies to help clarify the potential issues and develop solutions
 - A new **Employer, Viability and Funding Working Group** has been created to consider these matters in detail and report thereon to the Management Panel
 - It has in the past for very mature employers created “**Designated Funds**” that have earmarked assets for some employers with very mature liability profiles
 - We are in the initial stage of developing unitisation
 - Phase 1 – Accounting Issues -
 - Phase 2 – Investment Issues – make the adoption of more employer specific investment strategies easier

5. SCHEME DESIGN

- 5.1 A critical issue in the reform process is maintaining membership and the sustainability of the LGPS. A sustainable scheme brings benefits to many parties, not least society as a whole, by encouraging pension saving and reducing demand for means tested benefits. Councillor Quinn wrote to the Chancellor, Chief Secretary and Secretary of State in February setting out the Management Panel’s views on this matter re the proposed increase in employee contributions.
- 5.2 It was good that more time and flexibility was allowed to consider the options for delivering the required 3.2% saving.
- 5.3 Our initial view of the way forward is:
- (i) the package approach is best and the smaller the proportion derived from increasing employee contributions the better with compensating savings found from those elements of the benefit package that members attach least value to;
 - (ii) the scope for offering choice to the member as outlined in the employers’ proposals may have merit, i.e. the option to pay higher contributions and retain the benefit package or to retain existing contributions with a compensating reduction in the benefit package. We see maintaining some flexibility in the future would also be beneficial, but the trade off is more complicated administration;
 - (iii) it would be good if the new scheme design built on the proposals to deliver the short term savings;

- (iv) there will be major communication issues in advising members (and employers) of the short term and 2015 changes. Survey evidence suggests that the membership of the LGPS (Hymans Robertson) has a very limited understanding of the issues and proposals. We believe our communications are a strength and we would be keen to help DCLG and/or LGG with member, employer and administering authority communications;
- (v) the increasing scale of cliff edges in the employee contribution bands is a cause for concern; and
- (vi) the scale of increase for the better paid employees has a disproportionate impact v other public sector schemes.

5.4 The Management Panel has been a long term supporter of a CARE approach for the LGPS.