Pension Fund Investment Board

12 November 2012

Agenda

The Pension Fund Investment Board will meet at **Shire Hall, Warwick** on **12 November 2012** at **10:00 am**

1. General

(1) Apologies

(2) Members' Disclosures of Pecuniary and Non-Pecuniary Interests.

Members are required to register their disclosable pecuniary interests within 28 days of their election of appointment to the Council. A member attending a meeting where a matter arises in which s/he has a disclosable pecuniary interest must (unless s/he has a dispensation):

- Declare the interest if s/he has not already registered it
- Not participate in any discussion or vote
- Must leave the meeting room until the matter has been dealt with (Standing Order 42).
- Give written notice of any unregistered interest to the Monitoring Officer within 28 days of the meeting

Non-pecuniary interests must still be declared in accordance with the new Code of Conduct. These should be declared at the commencement of the meeting.

(3) Minutes of the previous meeting and matters arising

2. Investment Performance for Q2 2012/13

3. Pension Fund Cashflow

4. Absolute Return Managers

5. Employer Modelling 2013 Valuation

6. Valuation Planning 2013

7. Kingsbury Parish Council - Confirmation of Membership

8. Any Urgent Items

JIM GRAHAM
Chief Executive
Shire Hall
Warwick

Membership of the Pension Fund in Investment Board
Councillors John Appleton, Chris Davis (Chair), Jim Foster, Robin Hazelton, and Brian Moss

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Minutes of the Pension Fund Investment Board held on 30 July 2012

Present:
Members
Councillors John Appleton, Chris Davis, Jim Foster, and Brian Moss

Officers
Dave Abbott, Democratic Services Officer
Neil Buxton, Pensions Services Manager
Mathew Dawson, Principle Accountant
John Galbraith, Senior Solicitor, Employment Team
Christine Gough, Senior Accountancy Assistant
Andrew Lovegrove, Group Accountant
Phil Triggs, Treasury and Pensions Group Manager

Invitees
Peter Jones, Independent Adviser
Paul Potter, Adviser, Hymans Robertson
Sarah Wilson, CEO and founder, Manifest
Lyndon Bolton, Client Director, Schroders
Anthony Doherty, Property Fund Manager, Schroders
Graeme Rutter, Co-Head of Property Multi-Manager, Schroders

No members of the public attended the meeting.

1. General

(1) Apologies

Apologies were received on behalf of Councillor David Wright.

(2) Members' Disclosures of Pecuniary and Non-Pecuniary Interests

Councillors John Appleton and Chris Davis declared personal interests as members of the Local Government Pension Scheme.

(3) Minutes of the previous meeting

The minutes of the meeting of the Pension Fund Investment Board meeting held on 21 May 2012 were agreed as a true record and were signed by the Chair.

Matters Arising:

Fund Manager Appointment Process

A shortlist of fund managers had been chosen and interviews were to be held on the 10th and 11th of September 2012.

Risk – Assessing Employer Finances (bottom of page 5)

The Chair asked for the issue to be addressed in more detail at the next meeting of the Pension Fund Investment Board to be held on the 12th of November 2012.

2. Presentation from Manifest – The Proxy Voting Agency

Sarah Wilson, CEO and Founder of Manifest, addressed the Board and advised the members that a central issue for the fund is promoting good corporate governance in the companies that it invests in. Following an increase in media scrutiny of financial matters and a growing public interest in the sector, groups like 'FairPensions', a charity that promotes responsible investment by pension funds and fund managers, are seeking more transparency over the voting records of pension funds. In response, Manifest recommended that Warwickshire County Council signed up to the Financial Reporting Council's UK Stewardship Code which sets out good practice that it believes institutional shareholders should aspire to. The fund already meets the standards of the code and becoming a signatory would signal Warwickshire's intent to be open and transparent to the public.

Manifest recommended the following actions points be considered by the Board:

2012 – Quarter 3

- Review frequency / content of fund voting disclosures
- FairPensions / media scrutiny of asset owners in view

2012 – Quarter 4

- Become a stewardship Code signatory as an asset owner
- Refresh Statement of Investment Principles to reflect Stewardship Code

2013 – Quarter 1

- Review voting policy in light of:
    - Policy issues flagged by Manifest deeper annual analysis
    - Governance code changes due in Q3

Officers noted that the pension fund's voting record was published online and it can be viewed at the following link: www.warwickshire.gov.uk/pensionstatement

The Chair thanked Sarah Wilson, CEO and Founder of Manifest, for her presentation to the Board.

3. Presentation from Schroder Property

Graeme Rutter, Co-Head of Property Multi-Manager at Schroders, addressed the Board and informed members that the commercial property market had been through an unprecedented period of market volatility. Uncertainty and economic weaknesses still persist and in response to that Schroders had repositioned their investment profile to better suit today's environment.

Anthony Doherty, Property Fund Manager at Schroders, addressed the Board and informed members that Schroders are now focussed on the UK and had a clear strategy that favoured income and core funds. It was noted that transaction costs have also had an impact on investment performance. The key aim over the past twelve months had been to reposition the risk profile to protect the fund.

The Chair thanked Lyndon Bolton, Anthony Doherty, and Graeme Rutter from Schroders for their presentation to the Board.

4. Investment Performance

Mathew Dawson, Principal Accountant, presented the report and informed the Board that the fund value was £1,183.2m at 30 June 2012, a slight decrease from the fund position of £1,205.3m that was reported at the previous meeting. The decrease was attributed to weak equity markets over the period.

Paul Potter, Advisor from Hymans Robertson, noted that there was a discrepancy between the figures being reported by fund managers and the figures being reported by the Bank of New York Mellon. The total fund level figures were still accurate but the relative performance of the fund managers wasn't consistent with what individual managers were reporting. It was agreed that the issue would be followed up immediately after the meeting.

5. Projection of Future Cash Flow

Phil Triggs, Treasury and Pensions Group Manager, presented the report which recommended that a cashflow management policy should be put in place that accounts for the following points:

- The cash balance maintained is not so large as to reduce the potential for future investment returns.
- The cash balance maintained is not so small so as to create a risk that the balance will be easily exhausted, and thus disinvestments will be required either frequently or at short notice.
- Assets are realised in the most efficient manner possible.

Officers would continue to regularly monitor short term cashflows, based on whole fund membership data.

Resolved

That the Board agreed the principles of a cashflow management policy as set out in the report.

6. LIBOR Investigation

The Board considered the report that outlined the impact of the London Interbank Offered Rate (LIBOR) investigation on the Warwickshire pension fund. Phil Triggs, Treasury and Pensions Group Manager, presented the report and informed the Board that the alleged manipulation of LIBOR had had no significant impact on the fund. The fund had no exposure to either the reported treasury losses or the relevant financial instruments.

Officers said they would inform the Board if there were any further developments in the future.

7. Local Government Pension Scheme 2014

The Board considered the report that detailed the central changes to the Local Government Pension Scheme. Neil Buxton, Pensions Services Manager, presented the report and informed members that, following the Hutton report and Union negotiations, the proposed changes to the scheme will be communicated to scheme members, employers, funds and other scheme interests. Unions will consult with their members over the proposals and the LGA will consult employers. Central Government confirmed that a favourable outcome to the consultations will enable them to move to a statutory consultation in the autumn.

Communicating the changes to the membership of the scheme was highlighted as one of the biggest challenges going forward. The Pensions team had worked closely with partner authorities to produce a leaflet that will be sent to all members of the scheme.

8. Academies Update

The Board considered the report that detailed the number of maintained schools converting to academy status. Neil Buxton, Pensions Services Manager, presented the report and highlighted Appendix A, which showed the status of all schools in Warwickshire. At the time that the report was published, 21 maintained schools and one free school have been admitted to the pension fund as academies. A further two conversions were set for September 2012.

Further updates will be presented to the Board as the situation evolves.

9. North Warwickshire Home Carers Pension Provision

The Board considered the report to confirm the admission agreement for the outsourcing of home care services in North Warwickshire. Neil Buxton, Pensions Services Manager, presented the report and informed members that approximately 35 members of the Local Government Pension Scheme would be transferred to Home Group Limited, trading as Stonham Services. The Fund's actuary has assessed an employer contribution rate of 16.5% and a bond of £102,000.

Resolved

That the Pension Fund Investment Board note the admission agreement for the outsourcing of home care services in North Warwickshire.

10. Warwick Schools Catering Contract (Class Catering Ltd)

The Board considered the report to confirm the admission of Class Catering Limited to the Warwickshire Pension Fund. Neil Buxton, Pensions Services Manager, presented the report and informed members that four schools in the Warwick area had appointed Class Catering Ltd to provide catering at the schools. Six employees were members of the Local Government Pension Scheme (LGPS).

Resolved

That the Pension Fund Investment Board note the admission of Class Catering Limited to the Warwickshire Pension Fund in respect of these three contracts.

11. WCC Direct Payment Services: Penderels Trust

The Board considered the report to confirm the admission of Penderels Trust to the Warwickshire Pension Fund in respect of the Direct Payment Services contract. Neil Buxton, Pensions Services Manager, presented the report and informed members that following a tendering process, Penderels Trust won the contract from the County Council to provide direct payment services with effect from 1 October 2012 for four years. The transfer of the service from the Rowan Organisation to Penderels Trust affects six existing members of the Local Government Pension Scheme (LGPS).

Resolved

That the Pension Fund Investment Board note the admission of Penderels Trust to the Warwickshire Pension Fund in respect of the Direct Payment Services contract.

12. Any Other Items

The Chair noted that this was Phil Triggs' last meeting of the Pension Fund Investment Board before he moved to Surrey County Council and wished him the best of luck and thanked him for his all of his hard work on behalf of Warwickshire County Council.

The Board rose at 12.45pm

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Chair

Item 2

Pension Fund Investment Board
12 November 2012

Investment Performance

Report of the Head of Finance

Recommendation

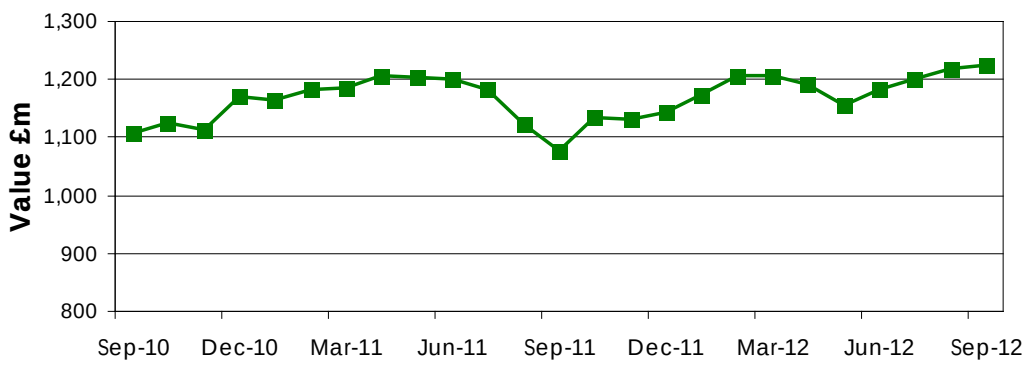
That the Investment Board note the fund value and investment performance for the second quarter in 2012/13 to 30 September 2012.

1. Fund Value at 30 September 2012

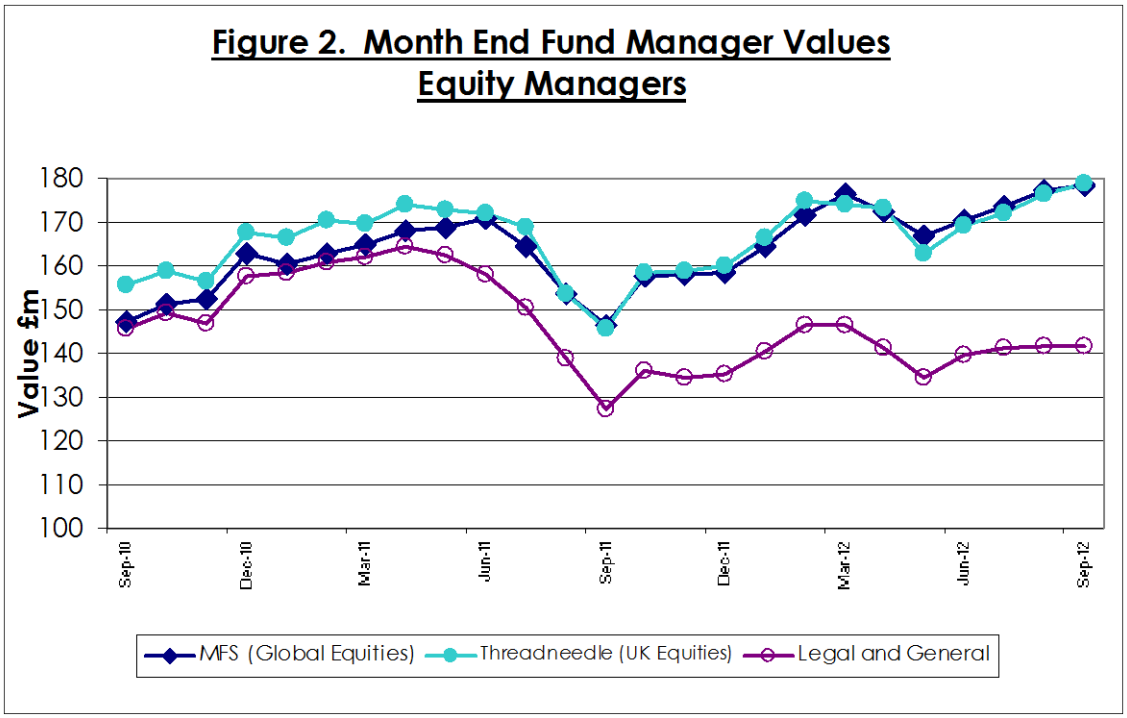
1.1 The report to the Board's meeting on 30 July 2012 gave the fund position of £1,183.2m at 30 June 2012.

1.2 The fund value was £1,223.9m at 30 September 2012.

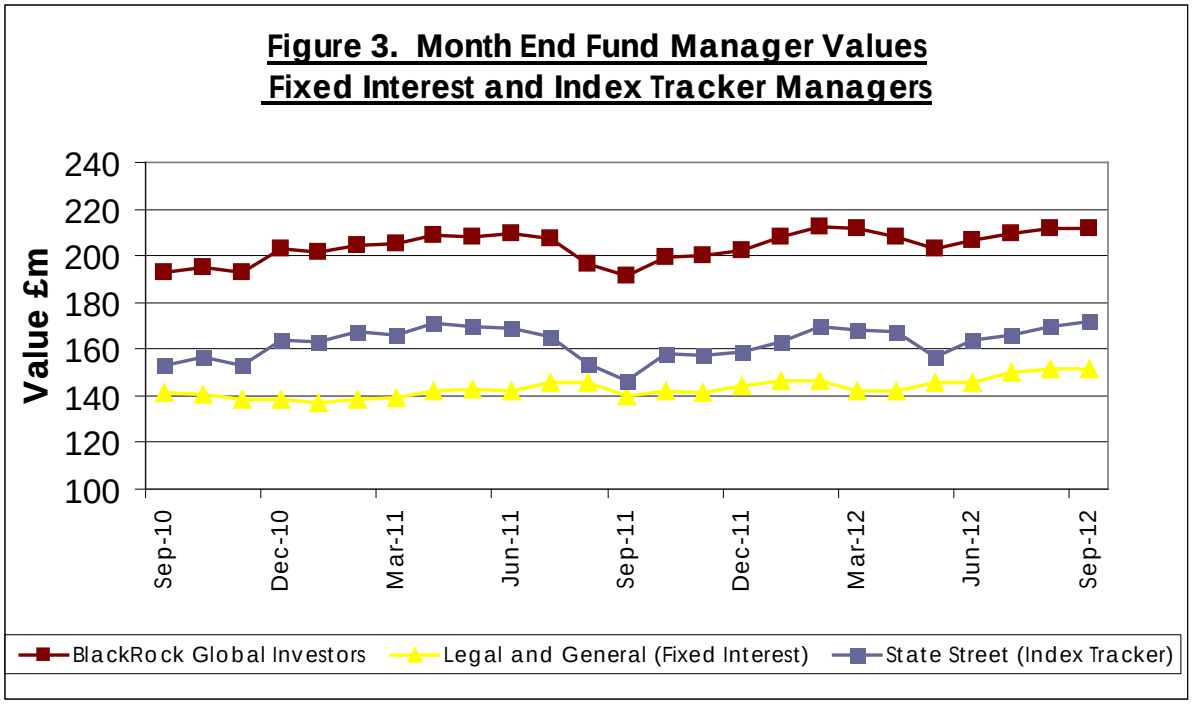
Figure 1. Total Fund Value Since 30 September 2010



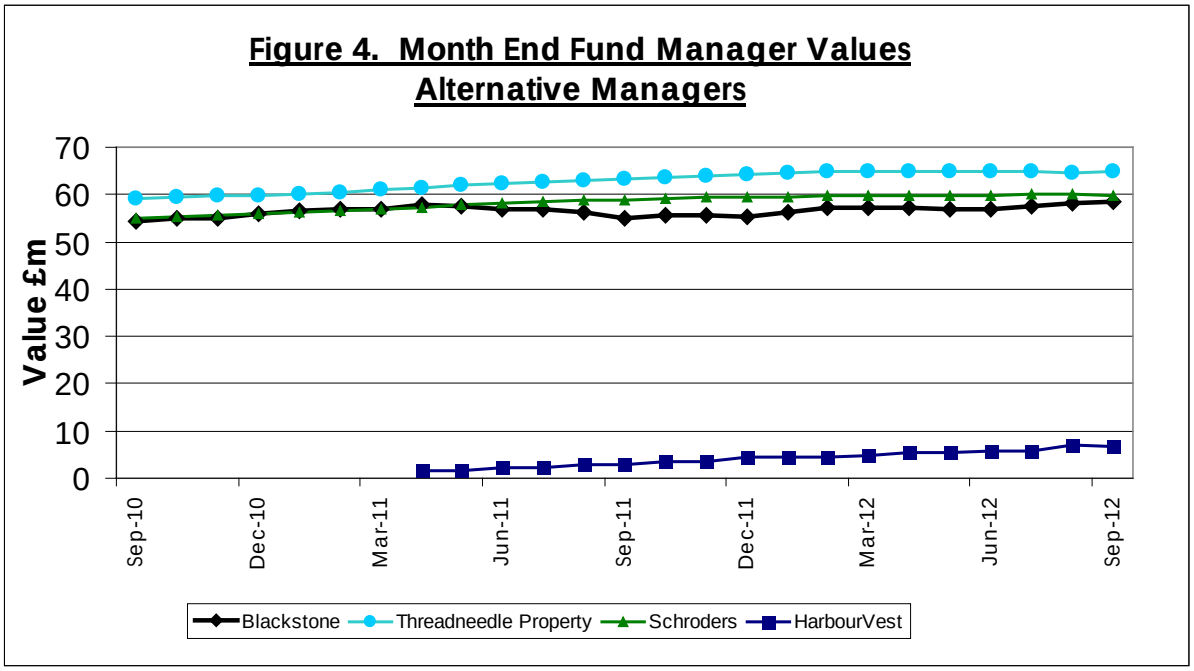
1.3 The values of the portfolios invested with the equity managers are shown in Figure 2.



1.4 The values of the portfolios invested with the Fixed Interest and Index-Tracker Managers are shown in Figure 3.



1.5 The values of the portfolios invested with alternative investment managers are shown in Figure 4.



2. Fund Asset Allocation

2.1 The performance of the Fund against its asset class benchmarks for the quarter ending 30 September 2012 is shown in Table 1.

Table 1: Fund Asset Allocation

Asset Class		Q/E Sep 2012 %	Fund policy %	Over/under weight %
Equity		**65.70**	**60.00**	**5.70**
	UK	36.00	30.30	5.70
	Europe (ex UK)	12.00	11.70	0.30
	North America	11.90	9.00	2.90
	Far East/Emerging Markets	5.80	9.00	-3.20
Fixed Income		**19.20**	**20.00**	**-0.80**
	UK corporate bonds	8.50	10.00	-1.50
	UK government bonds	5.60	5.00	0.60
	UK index linked bonds	5.10	5.00	0.10
Hedge Funds		**4.80**	**5.00**	**-0.20**
Private Equity		**0.60**	**5.00**	**-4.40**
Property		**9.30**	**10.00**	**-0.70**
Cash		**0.40**	**0.00**	**0.40**
Total		**100.00**	**100.00**	**0.00**

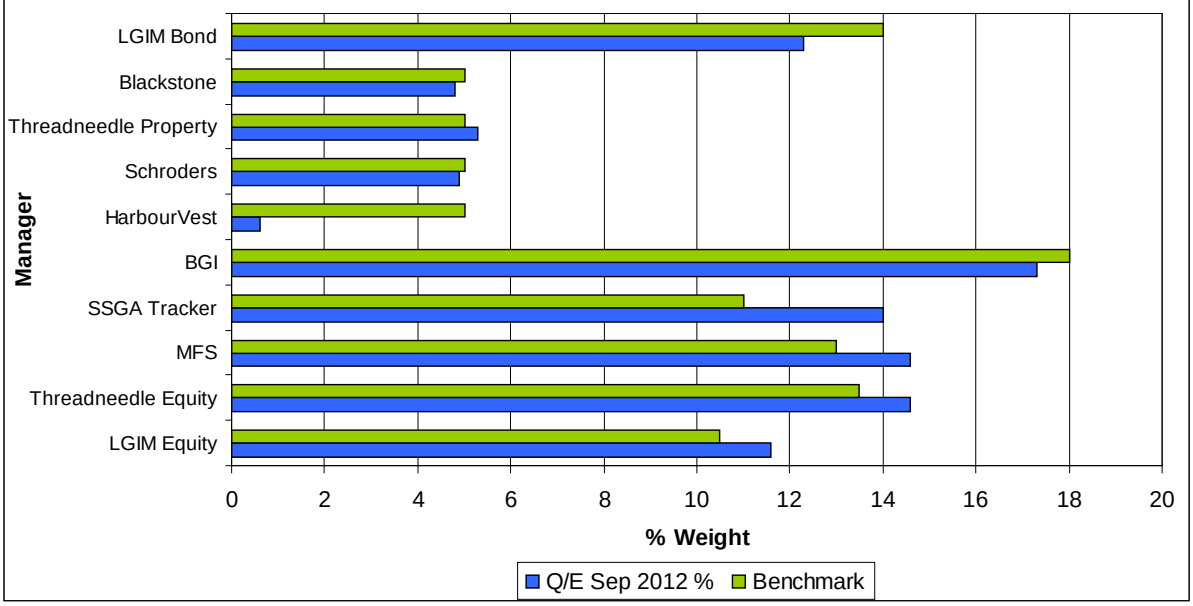
2.2 The fund managers' asset allocation against the benchmark for the quarter ending 30 September 2012 is shown in Table 2.

Table 2: Fund Asset Allocation by Manager

Manager	Benchmark	Q/E Sep 2012 %	Variance
LGIM Equity	10.5	11.6	1.1
Threadneedle Equity	13.5	14.6	1.1
MFS	13.0	14.6	1.6
SSGA Tracker	11.0	14.0	3.0
BGI	18.0	17.3	-0.7
HarbourVest	5.0	0.6	-4.4
Schroders	5.0	4.9	-0.1
Threadneedle Property	5.0	5.3	0.3
Blackstone	5.0	4.8	-0.2
LGIM Bond	14.0	12.3	-1.7
Total	100.0	100.0	0.0

2.4 Fund asset allocation against each manager is shown in Figure 5.

Figure 5. Manager Allocation - Quarter Ending 30 September 2012



2.5 HarbourVest will not be fully subscribed for some time as funds will be drawn down when the manager periodically requests the instalment payments.

3. Fund Performance

3.1 The performance of the Fund against its asset class benchmarks for the quarter ending 30 September 2012 is summarised in the table below.

Table 3: Performance by Asset Type

Asset Type	Benchmark Measure	Q/E Sep 2012 %	Benchmark %	Variance %
Equity				
United Kingdom	*Total Fund UK Composite*	4.96	4.65	**0.31**
Europe ex UK	*FTSE AW Dev Europe ex UK*	6.72	6.56	**0.16**
North America	*FTSE AW Dev North America*	3.72	3.54	**0.18**
Japan	*FTSE World Japan*	-3.34	-3.58	**0.24**
Pacific Basin ex Japan	*FTSE AW Developed Asia Pacific (ex Japan)*	7.43	7.43	**0.00**
Emerging Markets	*Total Fund Emerging Markets Composite*	5.55	4.65	**0.90**
Fixed Income				
UK Corporate Bonds	*iBoxx Sterling Non-Gilts*	5.74	5.67	**0.07**
UK Government Bonds	*FTSE UK Government All Stocks*	2.40	1.14	**1.26**
UK Index Linked Bonds	*FTSE UK Government Linked Gilts*	-2.60	-2.64	**0.04**
Alternatives				
Property	*Property Benchmark*	0.13	0.39	**-0.26**
Hedge Funds	*Hedge Funds Benchmark*	3.20	1.59	**1.61**
Total WCC Fund	***WCC Total Fund Benchmark***	**3.68**	**3.51**	**0.17**

3.2 Overall, the fund out-performed the benchmark by 0.17%. There was out-performance in nine asset classes.

3.3 One asset class under-performed their benchmark and one equalled their benchmark in the quarter.

3.4 The performances of managers against their benchmarks for the quarter ending 30 September 2012 were:

Table 4: Performance by Fund Manager

Manager	Benchmark Measure	Q/E Sep 2012 %	Benchmark %	Variance %
BlackRock Global Investors		2.33		**-0.72**
	BlackRock Benchmark		3.05	
MFS		4.69		**1.16**
	Global Equity Benchmark		3.53	
State Street Tracker		4.72		**0.03**
	FTSE All-Share		4.69	
Threadneedle		5.51		**0.82**
	FTSE All-Share		4.69	
Legal and General (Global Equities)		4.34		**0.48**
	LGIM Benchmark		3.86	
Legal and General (Fixed Interest)		4.07		**0.68**
	LGIM Benchmark		3.39	
Threadneedle Property		0.00		**-0.38**
	Threadneedle Property Benchmark		0.38	
Schroders Property		-0.05		**-0.46**
	Schroders Property Benchmark		0.41	
Blackstone Hedge		3.20		**1.61**
	Blackstone Hedge Benchmark		1.59	
Total		**3.68**		**0.17**
	WCC Total Fund Benchmark		**3.51**	

Source: BNY Mellon

3.4 Overall the fund out-performed its overall benchmark by 0.17%.

3.5 Twelve months data on the performance of the managers is available. The performance of managers against their benchmark over this period is shown below.

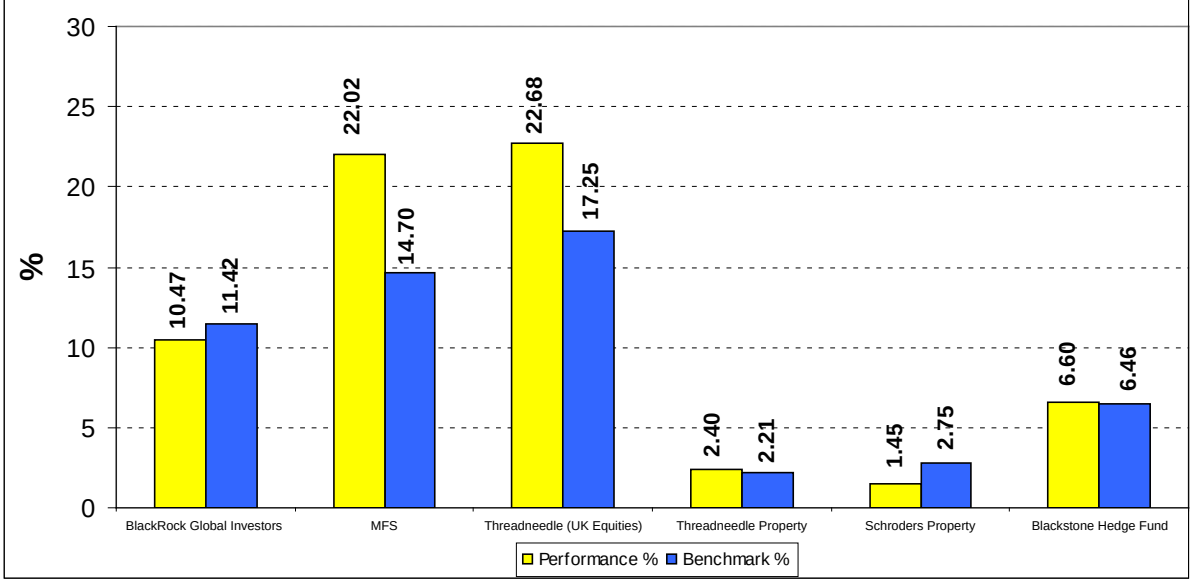
Table 5: Fund Manager Performance to Date

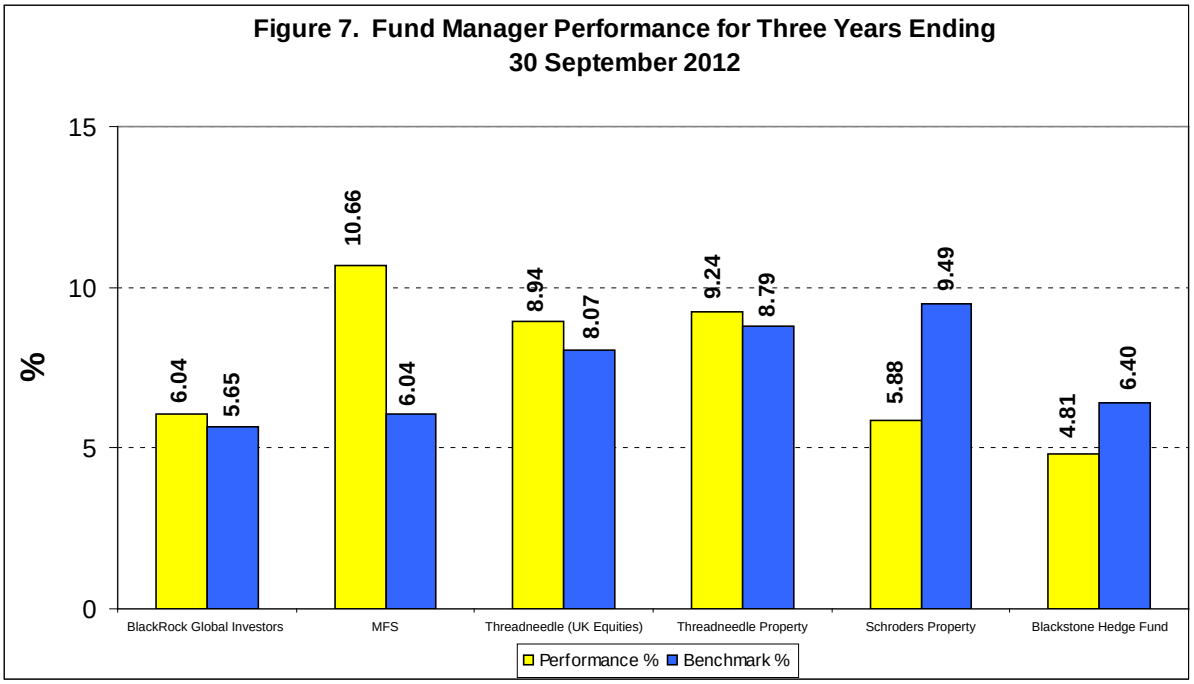
Manager	Variance Q/E Dec 11 %	Variance Q/E Mar 12 %	Variance Q/E Jun 12 %	Variance Q/E Sep 12 %
BlackRock Global Investors	**0.08**	**-0.25**	**0.00**	**-0.72**
MFS	**2.16**	**2.36**	**0.87**	**1.16**
State Street	**0.06**	**0.04**	**0.00**	**0.03**
Threadneedle	**1.55**	**2.58**	**-0.08**	**0.82**
Legal and General (Global Equities)	**0.32**	**0.08**	**-0.27**	**0.48**
Legal and General (Fixed Interest)	**-0.29**	**0.61**	**-0.36**	**0.68**
Threadneedle Property	**-1.22**	**-2.41**	**-0.25**	**-0.38**
Schroders Property	**-1.85**	**-2.67**	**-0.27**	**-0.46**
Blackstone Hedge	**-0.80**	**1.70**	**-2.34**	**1.61**
Total	**0.16**	**0.58**	**-0.24**	**0.17**

Source: BNY Mellon

3.6 Annualised return for the fund managers to 30 September 2012 is summarised in Figure 6. The three year annualised return is summarised in Figure 7.

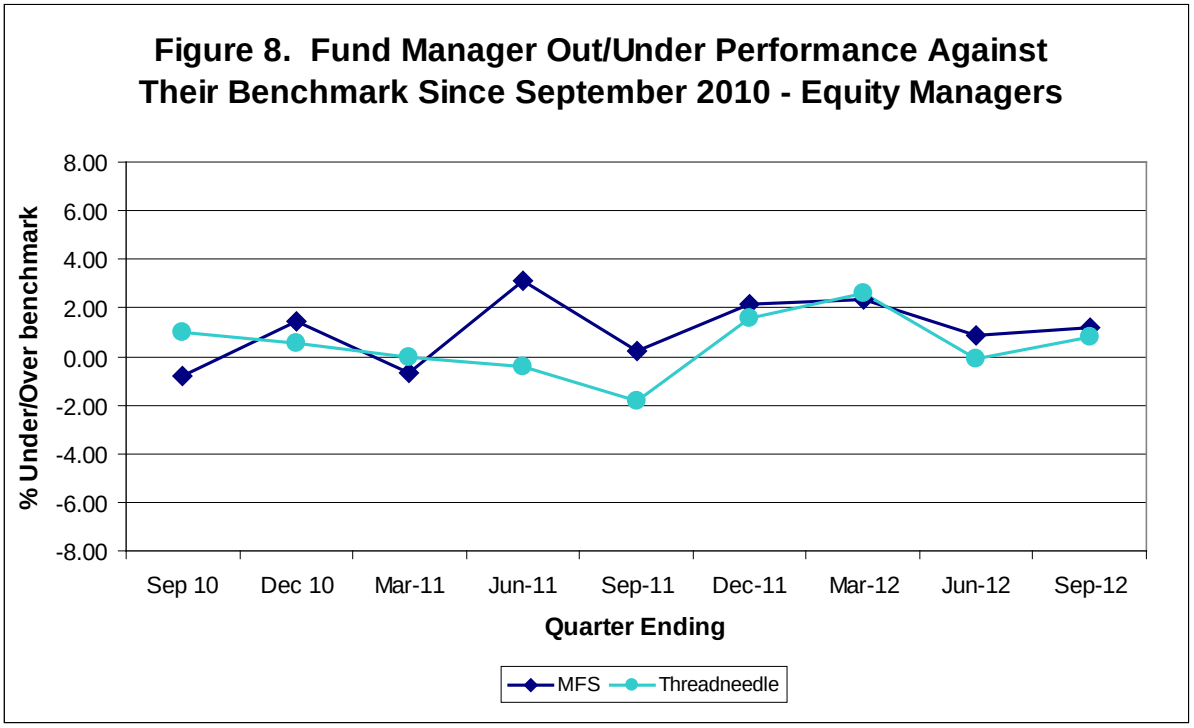
Figure 6. Fund Manager Performance for the Year Ending 30 September 2012

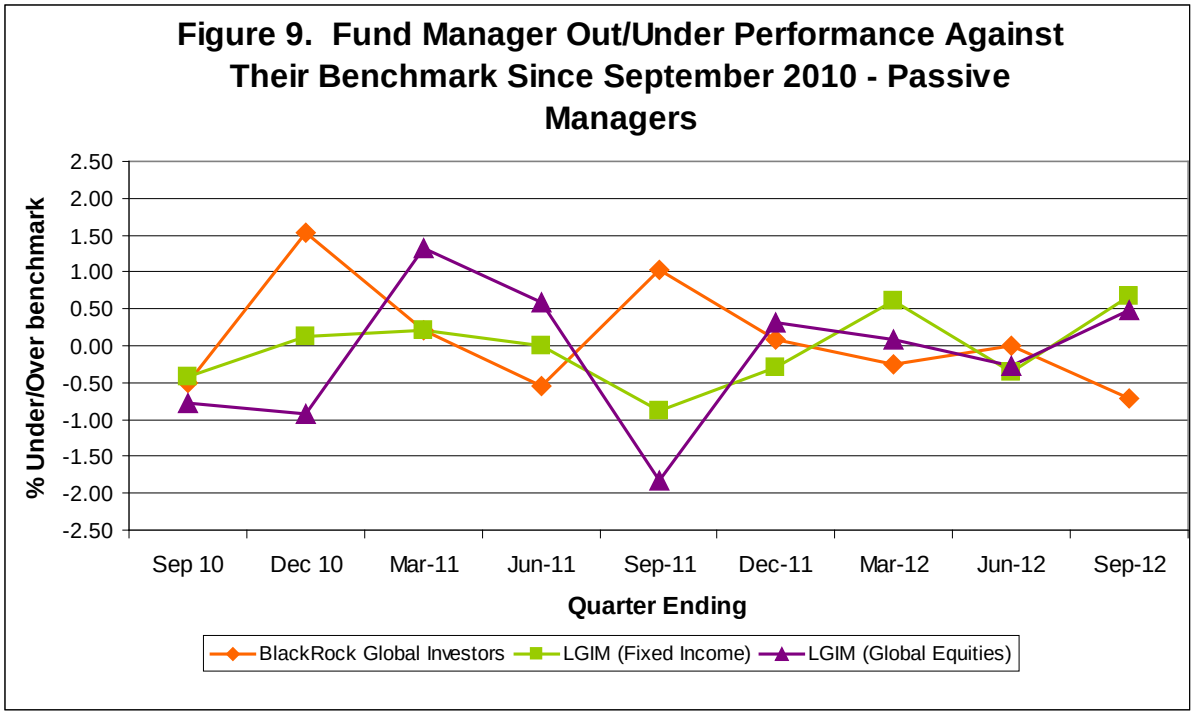




Source: BNY Mellon

3.8 Fund Manager performances against their benchmarks are summarised in Figures 8 and 9.





Source: BNY Mellon

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Chair	Cllr Chris Davis	cllrdavis@warwickshire.gov.uk

Item 3

Pension Fund Investment Board
12 November 2012

Pension Fund Cash Flow

Recommendation

That the Board approves the proposal set out in paragraph 4.1 of the report.

1. Introduction

1.1 The Fund's assets are invested across a range of different pooled and segregated mandates. With segregated mandates, any income which arises can, in principle, be paid over to the Fund rather than being available to the manager for re-investment. With pooled funds, units tend to be either 'distribution' or 'accumulation' units. There is no income paid out from accumulation units.

1.2 The advantage of drawing down the income from investments is that the manager is not forced to sell assets to meet the regular cash outgoings of the Fund. Where a manager is invested in a long term asset class such as equities which may exhibit significant volatility over shorter time periods, it is important to avoid having to sell assets at what might be a low point in markets as the portfolio is then smaller when the positive returns come through in the future.

1.3 The current mandates with managers require that any positive cash flows from investment activities are used by the managers to acquire further investment. These positive cash flows arise from two main activities, investment income and realised profit/loss. In addition we also recognise a third class of investment return in the form of unrealised profit/loss on investments.

Investment income

1.4 For 2011/12 the fund received investment income of some £13.6 million (2010/11 £10.2 million). This is in effect all of the dividends / interest received on the funds various investments. Attached at **Appendix B** is a copy of Note 18 in the funds 2011/12 annual accounts showing the analysis by investment type.

Realised profit/loss

1.5 For 2011/12 the realised profit on disposal of investments totalled £16.2 million. **Appendix B** includes a copy of note 5 of the 2011/12 pension fund accounts. This represents the difference between the cost and the disposal price achieved. This can also be described as “gains”. At present the mandates in place with managers requires them, within certain parameters, to re invest the sale proceeds (along with the profit /loss) in to appropriate new investments.

Unrealised profit /loss

1.6 For 2011/12 the unrealised profit on investments totalled £14.9 million. This reflects the uplift in the market price of investments compare to the opening valuation at the beginning of the financial year rather than a positive cash flow.

1.7 In summary the total income / profit for the fund in 2011/12, amounted to £44.7 million, of which £29.8 million relates to positive cash flows. As reported to the July 2012 meeting of the investment board, the fund is likely to go cash flow negative at some point in the next few years. This is dependant on decisions by the employers within the scheme, but in the current climate it is prudent to assume that the majority of the major employers will not be looking to increase employee numbers.

1.8 The proposal is to look to amend the mandates of managers to allow the fund to request that investment income could be paid to the fund rather than being re invested.

2. Fund Managers

Passive Managers

2.1 The funds passive managers are, Legal and General (“L&G”), BlackRock, and State Street. Distribution units are not available for these funds, though L&G do make available a facility whereby units can be sold at a mid-price (i.e. at no cost) up to a maximum value equivalent to the notional income received on the investments. This facility is available for the both the equity and bond funds.

Active Managers

2.2 The fund has two active segregated equity managers, a UK equity mandate managed by Threadneedle and a global equity mandate, managed by MFS. The Fund has the option of drawing this income, rather than it being re-invested by the managers.

2.3 The Fund has two property mandates managed by Threadneedle and Schroders. The investment with Threadneedle is in a pooled fund where only accumulation units are available. However, the Schroders fund-of-funds mandate is a segregated portfolio of underlying fund holdings, some of which produce income which is available for withdrawal.

2.4 The Fund also holds shares in a Fund of Hedge Fund mandate, managed by Blackstone Alternative Asset Management. There is no option for drawing down income from the shares.

2.5 **Appendix A** summarises the funds mandates and highlights where income is available.

New Managers

2.5 JP Morgan has created an income (distributing) share class for the JPM Strategic Bond Fund, although it is not yet launched (i.e. the share class is available to invest in but as yet this facility has not been utilised). Therefore, the estimated annual income quoted below is based on a similar share class, as a proxy. Barings do not offer income units in the Dynamic Asset Allocation Fund.

3. Estimated Annual Income

3.1 Table 1 summarises the estimated amount of income available from each fund manager, based on forecast data from the respective fund managers.

Table 1: Estimated Available Annual Income

Manager	Estimated Available Annual Income (£m)
L&G (Equities and Fixed Income)	**5.9**
Threadneedle (UK Equities)	**6.0**
MFS (Global Equities)	**3.8**
Schroders	**1.8**
JP Morgan	**1.7**
Total	**19.2**

3.2 Of the total amount in Table 1 it is assumed at this stage that around £10m will be required to meet the funds cash requirement in 2013/14.

3.3 The income will not be generated at an even rate throughout the year from the segregated mandates. Many UK companies, for example, have December year-ends and will pay their main final dividends between June and September 2013 and smaller dividends between December 2013 and March 2014. However, the indications from the managers are that the variations should not be substantial.

3.4 The Fund will be investing in income units for the new JP Morgan bond fund investment which will permit income withdrawal if necessary.

4. Proposal

4.1 Income will be drawn initially from L&G and Threadneedle (UK Equities) L&G are readily set up for this drawdown process through their notional income facility and this will be implemented by officers as will the process for drawing down the income from Threadneedle. Income would be available on a monthly basis from L&G, and on a quarterly basis from Threadneedle.

4.2 In the event of a large cash surplus building up in the funds current account, there is the option to instruct fund managers to suspend the distribution of income.

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Strategic Director	David Carter	davidcarter@warwickshire.gov.uk
Chair	Cllr Chris Davis	cllrdavis@warwickshire.gov.uk

Appendix A

Manager	Fund	Income Available?
L&G	Range of pooled bond and equity funds	Yes, 'notional dividend income facility' exists. This enables a regular income to be drawn at no cost (mid-market price) on a monthly basis. No income is available from the overseas equity funds.
BlackRock	Fund invests in Aquila Life range of funds.	No distributing share class for Defined Benefit schemes.
State Street	UK Equity Index Fund	No distribution facility available
MFS	Global Equity – segregated mandate	Yes
Threadneedle	UK Equity-segregated mandate	Yes, dividends would be swept into a separate income account and instruction given to custodian to pay income on a quarterly basis.
Threadneedle	UK Property Pension Fund – pooled fund	No distributing share class available
Schroders	UK Property Multi-Manager- segregated portfolio of pooled funds	Yes, 80% of income available for distribution
Blackstone	Fund of Hedge Fund	No distributing share class available

Appendix B

1. Realised and Unrealised Profit as published in Note 5 to the accounts 2011/12

	Value 1 April 2011 £ millions	Purchases at cost £ millions	Sales proceeds £ millions	Realised profit or loss (-) £ millions	Unrealised profit or loss (-) £ millions	Increase in debtors or (creditors) £ millions	Value 31 March 2012 £ millions
Fixed interest securities	5.3	0.0	0.0	0.0	0.9	0.0	6.2
Stocks and shares	328.2	130.2	-121.5	11.7	-4.9	0.0	343.7
Managed funds	837.0	25.2	-37.6	4.6	18.9	0.0	848.1
Cash and deposits	12.5	40.1	-42.2	0.0	0.0	-4.6	5.8
Other investments	1.7	0.2	-4.9	-0.1	0.0	4.6	1.5
Total	**1,184.7**	**195.7**	**-206.2**	**16.2**	**14.9**	**0.0**	**1,205.3**

Realised and unrealised profits added value of £31.1m (£16.2m+£14.9m) in the financial year 2011/12.

2. Investment Income analysis as published in Note 18 to the accounts 2011/12

2010/11 £000	Investment Income	2011/12 £000
5.9	Cash - UK - From administration of the Fund	5.2
23.3	Cash & Other Investments - UK - Fund Mgrs	-18.2
0.0	Cash & Other Investments - Overseas	1.3
4,667.9	Equities - UK	6,637.3
1,042.0	Equities - North America	1,264.6
1,391.3	Equities - Europe	1,576.6
317.2	Equities - Japan	288.4
114.6	Equities - Pacific (Ex Japan)	75.0
192.2	Equities - Emerging Markets	78.4
89.6	Stock Lending	47.8
2,311.4	Managed Funds - UK	2,263.7
122.4	Managed Funds - Overseas	1,316.9
10,277.8		**13,537.2**

Total investment income across all asset classes totalled £13.6m in the financial year 2011/12.

Item 4

Pension Fund Investment Board
12 November 2012

Absolute Return Managers

Recommendation

That the Board approve the current position with regard to the ongoing fund manager appointment process.

1. Introduction

1.1 This paper considers the implementation of the new investment arrangements following the appointment of Barings to manage a multi-asset absolute return mandate, and JP Morgan to manage an absolute return bond mandate.

2. Asset Allocation

2.1 At the board meeting on 21 May 2012, the Pension Fund Investment Board decided that the 5% allocation to the new Multi-Asset Absolute Return mandate should be funded from equities and that the 5% allocation to the new Absolute Return Bond mandate should be funded equally from equities and government bonds (gilts).

2.2 In Hymans Robertson's subsequent review of investment strategy, it was recommended that the relative allocations between UK and overseas equities should move from a ratio of 50:50 towards 40:60, reflecting the very concentrated nature (in company terms) of the UK equity market and the benefits of a better diversified global equity portfolio. The implication of this change on the fund asset allocation as a whole is shown in **Appendix A**.

2.3 It is intended that the full private equity allocation of 5% will be built up at the expense of UK equities though this may take a few years until the programme is fully established. In the meantime, the UK equity allocation will tend to be overweight to its final target.

3. Funding the New Fund Managers

JP Morgan – Strategic Bond Fund (Absolute Return Bonds)

3.1 The bond mandate will be funded 50% from fixed interest gilts and 50% funded from UK Equities. The gilts will be sold from the L&G passive bond mandate. This is because the Fund's other bond manager, BlackRock, does not hold a sufficient amount of gilts in their portfolio in order to provide the amount needed. The remaining 50% of assets required to fund the mandate

comes from the sale of equities from the State Street UK equity passive mandate.

Barings – Dynamic Asset Allocation Fund (Multi Asset Absolute Return)

3.2 The multi asset mandate will be 100% funded from UK Equities. It is propose that these funds are sourced from the State Street UK Equity passive mandate.

3.3 Threadneedle's UK Equity mandate will remain unchanged for the present. The managers long perm performance on this mandate has been reasonably good and it is likely to be more cost effective to raise assets from a passive manager than make substantial withdrawals from the active mandate.

Transition manager

3.4 The Fund's transition manager, Blackrock, will be asked to manage the necessary transfers of assets.

Manager Allocations

3.5 **Appendix B** shows the impact of incorporating the changes above to the State Street and L&G bond weightings, and the establishment of the absolute return bond and multi-asset absolute return allocations.

4. Summary and Conclusions

4.1 The State Street UK equity allocation will be reduced by 7.5% in order to fund the new mandates. This will reduce the UK/overseas equity targets from 50:50 to approximately 42.5:57.5 to provide a better diversified portfolio of equity investments.

4.2 The L&G bond allocation will be reduced by 2.5% to partially fund the new Absolute Return Bond mandate with JP Morgan.

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Appendix A

	Current Actual (%)	Current Target (%)	New Target (%)
Equities	**64.8**	**60.0**	**52.5**
UK	34.3	30.0	22.5
Overseas Equities	30.5	30.0	30.0
Private Equity	**0.5**	**5.0**	**5.0**
Property	**10.5**	**10.0**	**10.0**
Hedge Funds	**4.8**	**5.0**	**5.0**
Multi-Asset Absolute Return	**0.0**	**0.0**	**5.0**
Bonds	**19.4**	**20.0**	**22.5**
Gilts	4.1	5.0	2.5
Index-Linked Gilts	5.4	5.0	5.0
Corporate Bonds	9.9	10.0	10.0
Absolute Return	0.0	0.0	5.0
Total	**100.0**	**100.0**	**100.0**

Appendix B

Manager and Mandate	Current target allocation (%)	Proposed target allocation (%)
L&G (Global equity – passive)	12.0	12.0
L&G (Bonds – passive)	**13.0**	**10.5**
BlackRock (Global Equity – passive)	10.5	10.5
BlackRock (Bonds – passive)	7.0	7.0
Threadneedle (UK Equity – active)	13.5	13.5
State Street (UK Equity – passive)	**11.0**	**3.5**
MFS (Global Equity – active)	13.0	13.0
Schroders (Property)	5.0	5.0
Threadneedle (Property)	5.0	5.0
Harbourvest (Private Equity)	5.0	5.0
Blackstone (Hedge Fund)	5.0	5.0
JP Morgan (Absolute Return Bonds)	**0.0**	**5.0**
Barings (Multi Asset Absolute Return)	**0.0**	**5.0**
Total	100.0	100.0

Item 5

Pension Fund Investment Board
12 November 2012

Employer Modelling 2013 Valuation

Recommendations

The Board authorises the Strategic Director for Resources to take the following actions:

1. That a modelling exercise for the whole fund is carried out with results presented at the February 2013 board meeting.

2. In the summer of 2013 further analytical work should be carried out on an employer by employer basis where necessary. The fees for individual employers would be £12,500 for the first employer and £7,500 for each subsequent employer

1. Introduction

1.1 ComPASS is a modelling tool developed by Hymans Robertson and allows for a link to be made between funding and investment strategies – this is particularly useful at valuation time. **Appendix 1** provides an example of the output from this tool. The four main financial criteria assessed are Prudence, Affordability, Stability and Stewardship

1.2 It's primary aim is to introduce a contribution stabilisation mechanism for employers that are long term and secure to avoid surprises, improve budgeting and make contributions more affordable. Some form of stabilisation may also be appropriate for less secure long term employers but perhaps with wider annual limits on the mechanism.

1.3 ComPASS would also test that adopting stabilisation does not impact on the funding level of the Fund materially in the long term.

2. Approach

2.1 The approach is to be completely open about the current funding level (based on current market conditions) rather than masking the true position by making alterations to assumptions. This also ensures that other shorter term employers in the Fund pay for their own benefit promises. The modelling helps to judge whether the long term plan still works, and makes short and long term risks more obvious.

2.2 ComPASS can test various funding strategies to illustrate their impact on the funding level and employer contribution rate over the long term. The likelihood of the various outcomes are quantified and shown graphically. ComPASS can

also illustrate the effect of both different contribution and different investment strategies.

2.3 The analysis from ComPASS provides a robust audit trail that will stand up to external scrutiny and provides evidence that the employer rates certified in the Rates and Adjustment Certificate are appropriate and have been tested.

2.4 Officers will need to work with the actuary to select which strategies to model – known as 'scenarios'. The actuary would typically use six different scenarios and assess the effect of each of these on the measures outlined above i.e. Prudence, Affordability, Stability and Stewardship. The starting point for each scenario will be the whole fund contributions at the 2010 valuation (17.6% of pay). The scenarios will then use various contribution rate ceilings (e.g. 25%) and stabilising rules (e.g. contribution limits based on +/- 1% of pay pa).

3. Proposal

3.1 That a modelling exercise for the whole fund is carried out shortly out with results presented at the February 2013 board meeting. Fees for this work would be £12,000.

3.2 In the summer of 2013 there will be further analytical work done on an employer by employer basis where necessary. The fees for individual employers would be £12,500 for the first employer and £7,500 for each subsequent employer.

4. Timetable

4.1 Table 1 below provides the proposed timescale for this work in conjunction with the 2013 valuation.

Table 1 – High level 2013 Valuation Planning Timetable

On going	Data Cleansing exercise
February 2013	Whole fund ComPASS modelling results to be discussed at board meeting
July 2013	Main valuation data provided to Hymans Robertson, further ComPASS work undertaken specific to employers if necessary.
October 2013	Whole fund results and indicative employer results to be ready for AGM
March 2014	Valuation signed off.

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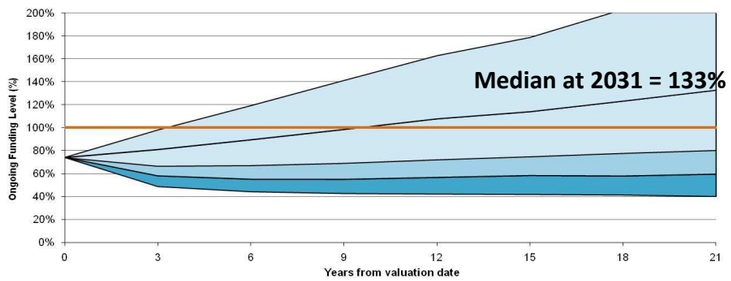
Appendix A

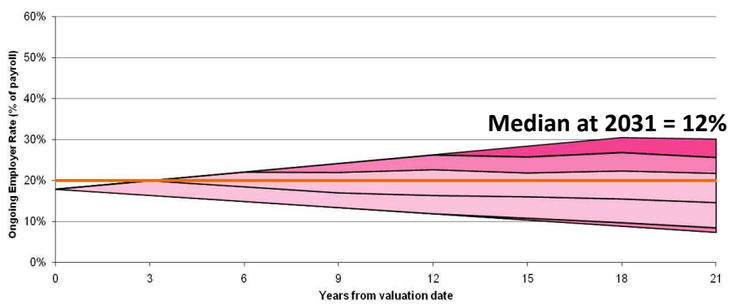
2010

- **ABC Pension Fund**
- **80%** funded at 2010
- Stabilisation rule - + 1% / -0.5%

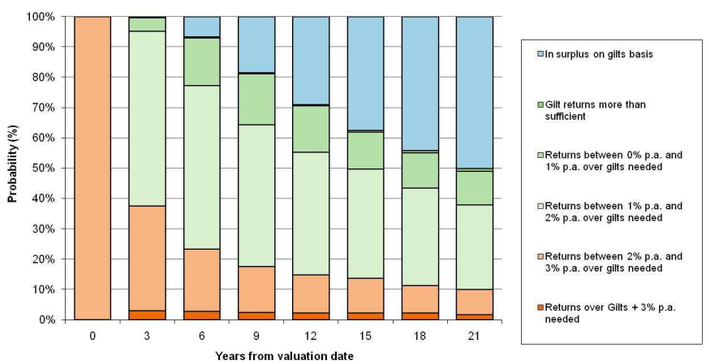
Stewardship



Affordability



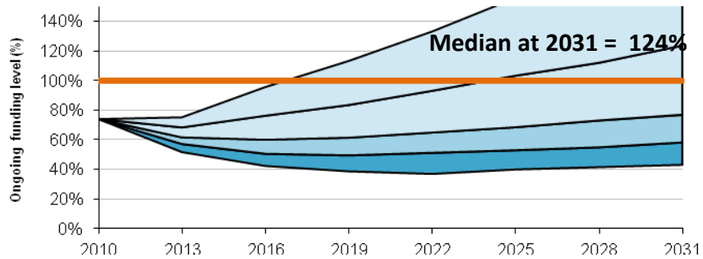
Prudence



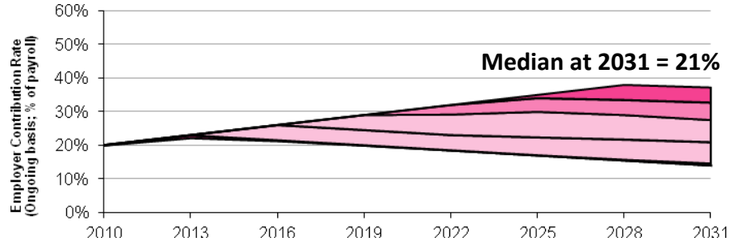
2012

- **ABC Pension Fund**
- **c70%** funded at 30 June 2012
- Stabilisation rule - +1% / -0.5%

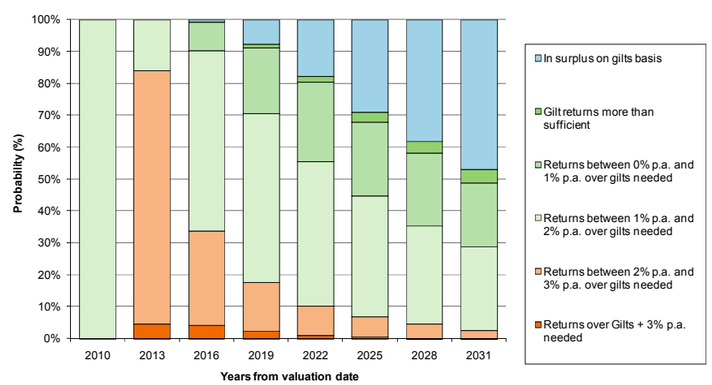
Stewardship



Affordability



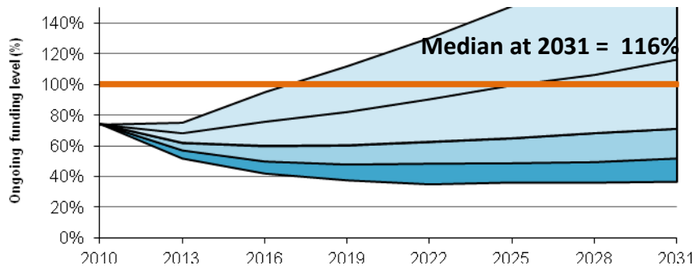
Prudence



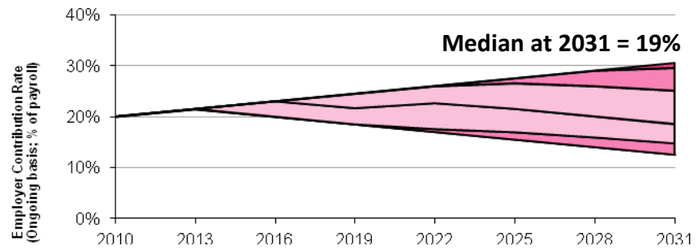
2012

- **ABC Pension Fund**
- c70% funded at 30 June 2012
- Stabilisation rule **- +0.5% / -0.5%**

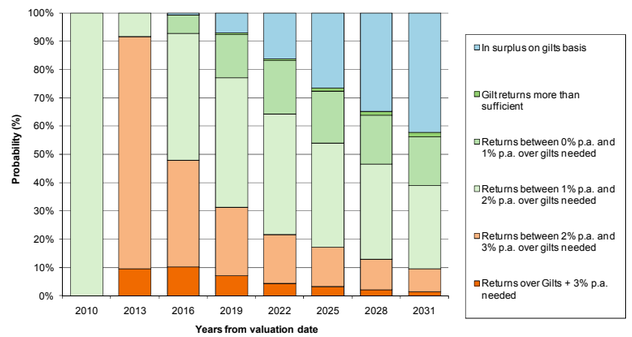
Stewardship



Affordability



Prudence

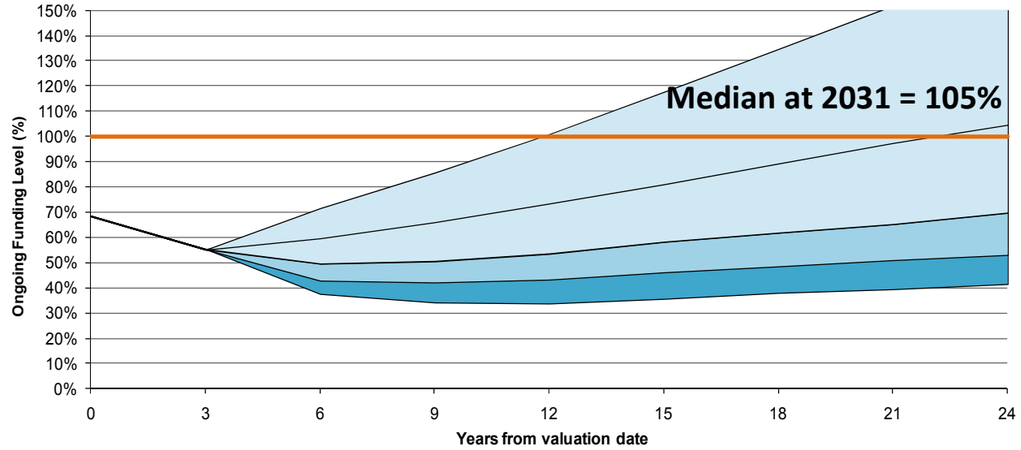


Appendix A

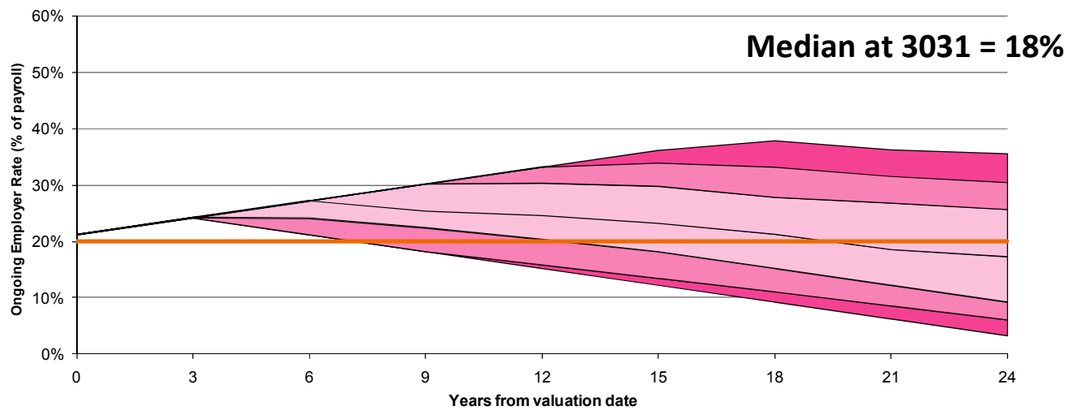
2010

- **61%** funded at 2010
- Stabilisation rule - Fixed until 2011, then +1% / -1%

<u>Stewardship</u> - Potential range in outcomes for the funding level over next 24 years



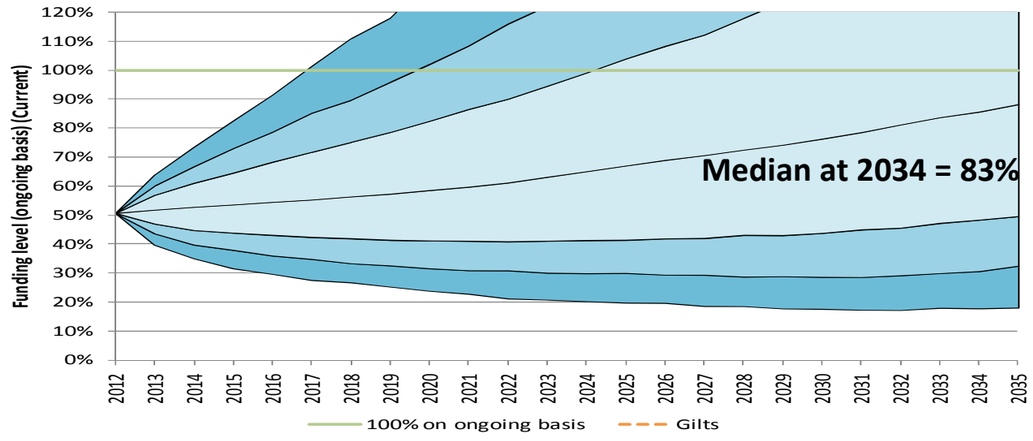
<u>Affordability</u> - Range of potential contribution rates over next 24 years



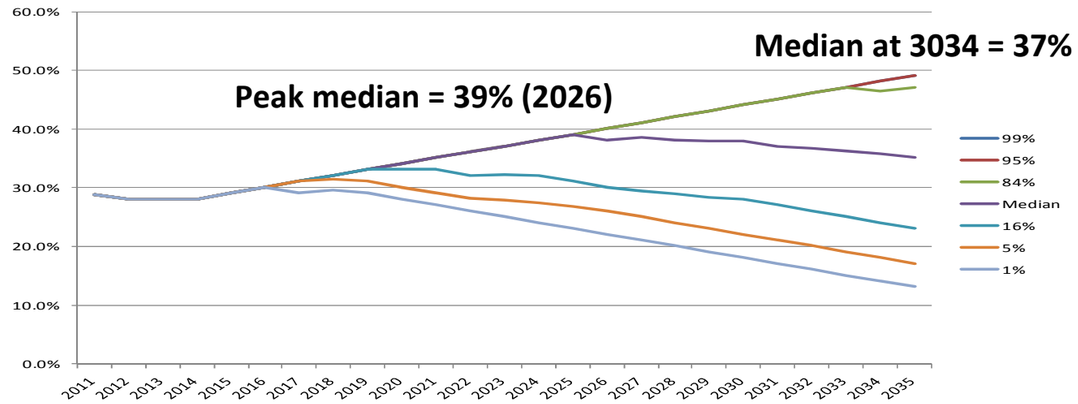
2012

- **C55%** funded at 2012
- Stabilisation rule - Fixed until 2011, then +1% / -1%

<u>Stewardship</u> - Potential range in outcomes for the funding level over next 24 years



<u>Affordability</u> - Range of potential contribution rates over next 24 years



Item 6

Pension Fund Investment Board
12 November 2012

2013 Valuation Planning

Recommendation

That the Board considers and decides which of the various options presented in the report it wishes to adopt for the 2013 actuarial valuation.

1. Introduction

1.1 Approaching the next actuarial valuation in 2013, there is a high probability that some employers will continue their programme of early retirements as has been the case since 2010. In the event of an early retirement, where benefits are not reduced, there is a "strain" payment to cover the cost of the pension being paid earlier than retirement age.

1.2 The 2010 valuation allowance for non ill health early retirements for four employers, whereby the strain costs were funded by additional contributions, this will cease from the 2013 valuation in favour of the options proposed in this report.

1.3 This report puts forward various ways of paying the early retirement strains in 1.2 above it will not alter the funds policy for remaining employers. The policy for charging strain costs to employers is set out in LGPS Regulations giving the Fund complete discretion.

2. Options for meeting strain costs

2.1 The fund actuary has outlined different ways of collecting strain costs. Each option has advantages and disadvantages to consider.

Option A – One off lump sum charged to the employer

2.2 This option is easy to understand, administer, and would mean that the full strain amount is paid as and when the early retirement occurs i.e. there is no spreading of the strain cost over time. It also gives the highest level of security to the fund as the full cost is met at retirement.

2.5 The disadvantages of this method would be an immediate financial strain on employers as it is a move from the current approach.

Option B – A chargeable lump sum spread over a number of years

2.6 As option A, but with the flexibility of paying the capitalised cost over a small number of years. The main implications would be an interest cost for the employer and additional time taken to recover the strain for the fund.

Option C - Spreading the costs over a small number of years through an increased contribution rate

2.7 As long as the period is short (e.g. 5 years or less), the security to the Fund of this approach is still reasonably strong although not as strong as option A or B. Some employers may like this option as costs are spread, the reduced period on offer is also in line with similar schemes that use this policy.

2.8 There is an inconsistency in timings of the strain and the money to meet this strain i.e. the strain will happen at the start of year 1 but the full amount of money paid to meet this strain will not be paid until year 3 or 5. This will mean that the Fund will subsidise the strain until the full amount is paid. Also there may be discontent between those employers who pay a strain cost up front and those who are allowed to spread the payment through contribution rates.

Option D – Paying a percentage of pensionable pay each year to pay for any strains that arise

2.9 The fund will receive payment in advance of meeting strains and will be simple to administer. This method may suit small employers in particular as there will be no 'one off' large payments to be made (although, from the Fund's perspective, this option is generally more appropriate for larger employers where the numbers of members taking early retirement are much more predictable from year to year).

2.10 This method would involve an increase to employer contribution rates which may cause some discontent. Also costs would be borne by the fund at each valuation to review the percentage being paid. A further disadvantage would be where strains arise early on when not enough money has been raised to meet them.

3. Other consideration

3.1 There may be transitional issues when work begins on the 2013 valuation. A decision will need to be made on whether any new funding approach applies only to new retirements or whether the new approach will apply to past retirements too.

4. Conclusion

4.1 The Fund has discretion over the way in which these strains are met. If security of benefits is key then option A involves the least risk. However the Fund may want to balance the relationship with employers by moving to an option, or a number of the proposed options that offer greater flexibility.

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Item 7

Pension Fund Investment Board
12 November 2012

Kingsbury Parish Council - Confirmation of Membership

Recommendation

That the Pension Board note that Kingsbury Parish Council has passed a resolution to become a scheduled body member of the Warwickshire Pension Fund.

1.0 Introduction

1.1 The Fund has been notified that Kingsbury Parish Council (the Council) has passed a resolution for the parish clerk to have access to the Local Government Pension Scheme (LGPS) administered by Warwickshire County Council.

1.2 The Council will be treated as part of the Parish and Town Council grouping for valuation purposes and will be required to contribute 19.1% of pensionable pay as the appropriate employer contribution rate.

1.3 Membership of the Warwickshire Pension Fund will be effective from 1 October 2012.

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Warwickshire County Council