

Democratic Services

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Date: 4 January 2011

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To: All Members of the Avon Pension Fund Committee - Investment Panel

Councillor David Bellotti (Chair), Councillor Gabriel Batt, Councillor Gordon Wood, Ann Berresford, Councillor Mary Blatchford and Bill Marshall

Chief Executive and other appropriate officers
Press and Public

Dear Member

Avon Pension Fund Committee - Investment Panel: Wednesday, 12th January, 2011

You are invited to attend a meeting of the **Avon Pension Fund Committee - Investment Panel**, to be held on **Wednesday, 12th January, 2011** at **9.30 am** in the **Council Chamber - Guildhall, Bath**.

The agenda is set out overleaf.

Yours sincerely

Sean O'Neill
for Chief Executive

If you need to access this agenda or any of the supporting reports in an alternative accessible format please contact Democratic Services or the relevant report author whose details are listed at the end of each report.

This Agenda and all accompanying reports are printed on recycled paper

NOTES:

- 1. Inspection of Papers:** Any person wishing to inspect minutes, reports, or a list of the background papers relating to any item on this Agenda should contact Sean O'Neill who is available by telephoning Bath or by calling at the Riverside Offices Keynsham (during normal office hours).
- 2. Public Speaking at Meetings:** The Council has a scheme to encourage the public to make their views known at meetings. They may make a statement relevant to what the meeting has power to do. They may also present a petition or a deputation on behalf of a group. Advance notice is required not less than two full working days before the meeting (this means that for meetings held on Wednesdays notice must be received in Democratic Services by 4.30pm the previous Friday)

The public may also ask a question to which a written answer will be given. Questions must be submitted in writing to Democratic Services at least two full working days in advance of the meeting (this means that for meetings held on Wednesdays, notice must be received in Democratic Services by 4.30pm the previous Friday). If an answer cannot be prepared in time for the meeting it will be sent out within five days afterwards. Further details of the scheme can be obtained by contacting Sean O'Neill as above.

- 3. Details of Decisions taken at this meeting** can be found in the minutes which will be published as soon as possible after the meeting, and also circulated with the agenda for the next meeting. In the meantime details can be obtained by contacting Sean O'Neill as above.

Appendices to reports are available for inspection as follows:-

Public Access points - Riverside - Keynsham, Guildhall - Bath, Hollies - Midsomer Norton, and Bath Central, Keynsham and Midsomer Norton public libraries.

For Councillors and Officers papers may be inspected via Political Group Research Assistants and Group Rooms/Members' Rooms.

- 4. Attendance Register:** Members should sign the Register which will be circulated at the meeting.
- 5. THE APPENDED SUPPORTING DOCUMENTS ARE IDENTIFIED BY AGENDA ITEM NUMBER.**
- 6. Emergency Evacuation Procedure**

When the continuous alarm sounds, you must evacuate the building by one of the designated exits and proceed to the named assembly point. The designated exits are sign-posted.

Arrangements are in place for the safe evacuation of disabled people.

Avon Pension Fund Committee - Investment Panel - Wednesday, 12th January, 2011

at 9.30 am in the Council Chamber - Guildhall, Bath

A G E N D A

1. EMERGENCY EVACUATION PROCEDURE

The Chair will draw attention to the emergency evacuation procedure as set out under Note 9.

2. DECLARATIONS OF INTEREST

3. APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

To receive any declarations from Members of the Committee and Officers of personal/prejudicial interests in respect of matters for consideration at this meeting, together with their statements on the nature of any such interest declared.

4. TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

5. ITEMS FROM THE PUBLIC - TO RECEIVE DEPUTATIONS, STATEMENTS, PETITIONS OR QUESTIONS

6. ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

To deal with any petitions or questions from Councillors and, where appropriate, co-opted and added members.

7. MINUTES: 11 NOVEMBER 2010 (Pages 5 - 8)

8. RECAP ON HEDGE FUND MANAGERS PAPER (Pages 9 - 62)

ENTER CLOSED SESSION

9. PRESENTATION BY SIGNET - CLOSED SESSION

10. PRESENTATION BY STENHAM - CLOSED SESSION

BREAK

11. PRESENTATION BY LYSTER WATSON - CLOSED SESSION

12. SUMMARISE CONCLUSIONS - CLOSED SESSION

RETURN TO OPEN SESSION

13. AGREE BRIEF FOR SRI REVIEW (Pages 63 - 66)

The Committee Administrator for this meeting is Sean O'Neill who can be contacted on

.

AVON PENSION FUND COMMITTEE - INVESTMENT PANEL

Minutes of the Meeting held

Thursday, 11th November, 2010, 1.30 pm

Members: Councillor David Bellotti (Chair), Councillor Gabriel Batt, Councillor Gordon Wood, Ann Berresford, Councillor Mary Blatchford and Andy Riggs (In place of Bill Marshall)

Advisors: Tony Earnshaw (Independent Advisor), Dave Lyons (JLT Benefit Solutions) and Jignesh Sheth (JLT Benefit Solutions)

Also in attendance: Liz Feinstein (Investments Manager) and Matthew Betts (Assistant Investments Manager)

15 EMERGENCY EVACUATION PROCEDURE

The Democratic Services Officer read out the procedure.

16 DECLARATIONS OF INTEREST

There were none.

17 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

Apologies were received from Bill Marshall, for whom Andy Riggs substituted.

18 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

19 ITEMS FROM THE PUBLIC - TO RECEIVE DEPUTATIONS, STATEMENTS, PETITIONS OR QUESTIONS

There were none.

20 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

21 MINUTES: 16 SEPTEMBER 2010

These were approved as a correct record and signed by the Chair.

22 EXCLUSION OF PUBLIC

RESOLVED that, having been satisfied that the public interest would be better served by not disclosing relevant information, and in accordance with the provisions of Section 100(A)(4) of the Local Government Act 1972, the public be excluded from the meeting for the following three items of business because of the likely disclosure

of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Act as amended.

23 REVIEW OF HEDGE FUND MANAGERS

The Investments Manager presented the report. She reminded Members of the framework for the review of hedge fund portfolios, which had been adopted by the Avon Pension Fund Committee at its meeting on 25 June 2010. Stage one was a review of the investment and operational performance of the five Fund of Hedge Fund managers. The Panel's comments on them would be fed into the workshop to be held in 1Q11. The workshop will also cover the strategic investment in hedge funds, the allocation to the underlying investment strategies and regulatory issues.

At this meeting the 2 of the hedge fund managers presented to the Panel with the other 3 presenting at the Panel's next meeting. To aid the Panel, JLT prepared a preliminary report on the hedge fund managers which was circulated as an exempt appendix to the agenda report.

Prior to the presentations Mr Lyons highlighted the key findings of the report to help focus the discussion with the managers.

Following discussion, it was **RESOLVED** to identify issues with the individual hedge fund managers to be incorporated into the review of the Fund's hedge fund investments.

24 MEET THE MANAGER - GOTTEX FUND MANAGEMENT

Richard Leibovitch (Chief Investment Officer, co-PM of Gottex Market Neutral Funds), Chris Hawkins (Managing Director, co-PM of Gottex Market Neutral Funds) and Michael Lorraine (Director Institutional Sales, Gottex Fund Management) presented to the Panel. Copies of their presentation were presented to Members.

The presentation covered the following:

- (i) investment philosophy and process
- (ii) Allocation to investment strategies and how they have actively managed the allocations
- (iii) investment performance over last 3 years
- (iv) Management of operational processes
- (v) changes introduced to investment and operational processes to manage the challenges of the last 3 years

The Chair thanked the team from Gottex for presenting to the Panel.

25 MEET THE MANAGER - MAN

Anthony Lawler (Head of Portfolio Management), Jonathan Howard (Senior Portfolio Manager) and Paul Dackombe (Head of Institutional Clients – UK) of MAN presented to the Panel. Copies of their presentation were presented to Members.

The presentation covered the following:

- (i) investment philosophy and process

- (ii) Allocation to investment strategies and how they have actively managed the allocations
- (iii) investment performance over last 3 years
- (iv) Management of operational processes
- (v) changes introduced to investment and operational processes to manage the challenges of the last 3 years

The Chair thanked the team from MAN for presenting to the Panel.

26 ALLOCATION TO PASSIVE UK EQUITIES

The Panel returned to open session.

The Investments Manager presented the report. The Avon Pension Fund Committee had decided at its meeting on 24 September 2010 that the Investment Panel should consider a further switch between the UK and overseas equities. This followed a discussion by the Committee of the sector and stock concentration within the UK equity indices.

At present the allocation within the equity portfolio was 45% UK equities to 55% overseas equities. Any potential switch would be implemented via the passively managed equity portfolios.

The report set out the impact in terms of the risk return profile of the Fund if the allocation to UK equities was incrementally reduced to 30%. There was discussion around the diversification benefits from increasing the allocation to global equities. Global equities increase the volatility from currency; however, the Fund is appointing a manager to hedge currency risk so the Panel concluded that this risk would be adequately managed. JLT advised that the diversification benefit of increasing the allocation to global equities to 70% would be to reduce volatility by around 0.1%. Appendix 1 of the report compared allocation to sectors and the top 10 stocks within the FTSE All Share and MSCI World indices. In particular, the global indices have higher allocation to technology and industrial sectors.

After discussion, the Panel **RESOLVED** to recommend to the Avon Pension Fund Committee that the allocation between UK and global equities should be switched from 45:55 to 30:70.

27 GLOBAL EQUITY TENDER

The Assistant Investments Manager gave a verbal report to Members. A full open tendering exercise had been undertaken. There had been 59 responses, which the evaluation process reduced to 4 following discussions with Officers and the Independent Advisor. Clarification meetings had been held with the 4 managers, three of whom were invited to attend the selection panel on 24 November 2010.

The meeting ended at 5.17 pm

Chair(person)

Date Confirmed and Signed

Prepared by Democratic Services

Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND INVESTMENT PANEL	
MEETING DATE:	12 January 2011	AGENDA ITEM NUMBER
TITLE:	REVIEW OF FUND OF HEDGE FUND MANAGERS	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
<p>List of Attachments:</p> <p>Exempt Appendix 1 – JLT’s Report on Hedge Fund Managers January 2011</p> <p>Appendix 2 – Background information on Signet</p> <p>Appendix 3 – Background information on Stenham</p> <p>Appendix 4 – Background information on Lyster Watson</p>		

1 THE ISSUE

- 1.1 Following the review of the Strategic Investment Strategy in June 2009, it was agreed that a formal review of the Fund’s investments in hedge funds be undertaken in 2010/11 once the mandates had been in place for three years. A Committee workshop has been arranged for 2 March 2011 where the strategic allocation to hedge funds and the managers will be reviewed.
- 1.2 Prior to the workshop, the Investment Panel have been asked to review performance of the individual Fund of Hedge Fund (FoHF) managers. The Panel met MAN and Gottex in November 2011 and the final three managers, Signet, Stenham and Lyster Watson will present to the Panel at this meeting.
- 1.3 JLT prepared a report for the meeting on 11 November 2011 that reviewed performance, operational and management issues as well as the managers’ exposure to the underlying investment strategies. This report has been updated for any new information (see Exempt Appendix 1). JLT’s initial findings are set out in 6.4. At this stage of the review, the focus is on the individual managers and not on the strategic decision to invest in hedge funds.
- 1.4 Appendices 2, 3 & 4 provide background information on the managers presenting at this meeting, Signet, Stenham and Lyster Watson.

2 RECOMMENDATION

That the Investment Panel:

- 2.1 **Identifies issues with the individual hedge fund managers to be incorporated into the review of the Fund’s hedge fund investments.**

3 FINANCIAL IMPLICATIONS

3.1 The budget provides for investment advice to review the hedge fund portfolio.

4 FRAMEWORK FOR REVIEW OF HEDGE FUNDS

4.1 The Investment Panel recommended the following framework for the review of the hedge fund portfolio:

- (1) Review of the managers by the Investment Panel
- (2) Strategic Review of allocation to hedge funds by the Investment Consultant
- (3) Review of regulation changes and potential impact on investment opportunities
- (4) Committee workshop in Q1 2011 to review hedge funds (covering 1-3 above).

5 CONTEXT - RECAP ON RATIONALE & STRUCTURE OF HEDGE FUND PORTFOLIO

5.1 In order to put the individual managers into context, the following briefly summarises the rationale for the hedge fund portfolio and the portfolio structure.

5.2 The Fund allocated 10% to fund of hedge funds and was seeking to generate consistent annual returns (net of fees) of LIBOR plus 4-6% with a volatility of less than 10%. The portfolio was to have a focus on capital preservation. The Fund was therefore looking for a relatively low volatility, low-medium return portfolio and given the nature of FoHF portfolios it was decided that more than one manager would need to be appointed in order to achieve the optimum volatility/return profile.

5.3 As a result the five FoHF managers were appointed, the combination of them providing the required volatility /return profile and a diverse exposure to underlying strategies. In particular, three of the managers, Signet, Gottex and Stenham were selected given their relatively low volatility profile, with commensurate lower return potential. MAN and Lyster Watson were selected as they had higher volatility and return objectives. Thus they would help the Fund achieve its return objective whereas as the lower volatility managers would provide capital protection and dampen overall volatility.

5.4 In addition, the five managers have different approaches to investing which means the overall portfolio will have a well diversified exposure to the main underlying investment strategies. *Please see JLT report (Exempt Appendix 1) for definition of investment strategies.*

5.5 MAN and Lyster Watson are multi-strategy managers meaning they are opportunistic and allocate capital across the full range of hedge fund strategies. The diversification within each portfolio will reduce volatility and help smooth returns over time.

5.6 Gottex, Signet and Stenham have more focussed approaches to investing. Stenham are a multi strategy manager but only invest in liquid investment strategies where they are not reliant on leverage to enhance returns. Therefore

they would expect to allocate most capital to long/short equity, macro, commodities and event driven strategies.

5.7 Gottex are a market neutral manager meaning they will not take any significant positions that rely on return being generated from market movements (i.e. do not bet on equity, bond, currency or commodity market trends). As a result they allocate capital to “relative value” and arbitrage strategies amongst others.

5.8 Signet focuses purely on fixed income and credit strategies; they will allocate to both market neutral and directional strategies within the fixed income and credit markets.

6 REVIEW OF INDIVIDUAL FUND OF HEDGE FUND MANAGERS

6.1 This review is in two parts: (i) a report by JLT and (ii) Panel meetings with each manager. These meetings and JLT’s report will form the basis for the assessment of the individual managers by the Investment Panel.

Report by JLT

6.2 JLT’s report in Exempt Appendix 1 provides analysis on each individual hedge fund manager. These managers have been managing assets on behalf of the Fund for just over three years, which has been a tumultuous period in financial markets and the global economy. The JLT report reviews what each manager might reasonably be expected of them against this backdrop. The report summarises their initial findings on each manager and highlights issues where the Panel may wish to obtain further assurance.

6.3 The report is set out as follows:

- (1) Section 1 – Investment Performance over last 3 years
- (2) Section 2 – Allocation to underlying investment strategies and how these have changed over time
- (3) Section 3 – Operational Structure and performance discusses how the managers have strengthened their operational and due diligence processes

6.4 **JLT’s initial findings** are summarised as follows (please refer to Executive Summary in Exempt Appendix 1, page 2 for full summary):

- (1) Performance has been disappointing as none of the managers have achieved their performance target since inception. However, this is mainly due to poor performance against target in 2008; performance has improved in 2009 and 2010. The investment return of the hedge fund portfolio has been significantly less volatile than the return from global equities.
- (2) As expected the managers have actively altered allocations between investment strategies in response to opportunities within their investment universe and have reduced exposure to strategies that relied on leverage to enhance return. However, JLT’s initial findings are that there is a risk that the highly diversified structure of some managers’ portfolios could dilute the overall contribution to return from the active management by the manager and therefore the Fund should review this issue. MAN’s portfolio is particularly diverse; however, they are in the process of reducing the number of underlying funds.

- (3) All the managers faced significant operational challenges in 2008/09 with regard to managing redemptions and liquidity of underlying investments. As a result all managers have reviewed their internal processes and managers have addressed areas identified as weak. JLT recommend that given the more challenging environment in which FoHF managers now operate, the Panel should conclude whether each of the managers has adequate resources and processes in place to meet these challenges.

Manager Meetings

6.5 At the meetings the Panel are asked to review performance of the FoHF managers, focusing on:

- (1) Their exposure to underlying investment strategies
- (2) The three year investment performance
- (3) Their operational / management performance, including changes introduced since 2008 financial crisis

6.6 MAN and Gottex presented to the Panel at the meeting on 11 November 2010. The other FoHF managers, Signet, Stenham and Lyster Watson will present at the Investment Panel meeting on 12 January 2011.

6.7 Appendices 2, 3 & 4 provide background information on Signet, Stenham and Lyster Watson, which should be read in conjunction with the report by JLT. Potential questions which cover areas the Panel may wish to focus on will be circulated at the presentations.

7 RISK MANAGEMENT

7.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

8 EQUALITIES

8.1 An equalities impact assessment is not necessary.

9 CONSULTATION

9.1 N/a

10 ISSUES TO CONSIDER IN REACHING THE DECISION

10.1 No decisions are being made. The issues being considered to make a recommendation to the Committee are contained in the report and comments are sought in the report.

11 ADVICE SOUGHT

11.1 The Council's Monitoring Officer (Council Solicitor) and Section 151 Officer (Divisional Director - Finance) have had the opportunity to input to this report and have cleared it for publication.

Contact person	Liz Feinstein, Investments Manager 01225 395306
Background papers	
Please contact the report author if you need to access this report in an alternative format	

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Access to Information Arrangements

Exclusion of access by the public to Council meetings

Information Compliance Ref: LGA-11-001

Meeting / Decision: Avon Pension Fund Investment Panel

Date: 12 January 2011

Author: Liz Feinstein

Report Title: Review of fund of hedge fund managers

Exempt Appendix Title:

Appendix 1 – JLT's Report on Hedge Fund Managers November 2010

Stating the exemption:

- 3. Information relating to the financial or business affairs of any particular person (including the authority holding that information).*

The public interest test has been applied, and it is concluded that the public interest in maintaining the exemption outweighs the public interest in disclosure at this time. It is therefore recommended that the committee resolve to exclude the public. The paragraphs below set out the relevant public interest issues in this case.

PUBLIC INTEREST TEST

If the Committee wishes to consider a matter with press and public excluded, it must be satisfied on two matters.

Firstly, it must be satisfied that the information likely to be disclosed falls within one of the accepted categories of exempt information under the Local Government Act 1972. Paragraph 3 of the revised Schedule 12A of the 1972 Act exempts information which relates to the financial or business affairs of the investment managers which is commercially sensitive to the investment managers. The officer responsible for this item believes that this information falls within the exemption under paragraph 3 and this has been confirmed by the Council's Information Compliance Manager.

Secondly, it is necessary to weigh up the arguments for and against disclosure on public interest grounds. The main factor in favour of disclosure is that all possible Council information should be public and that increased openness about Council business allows the public and others affected by any decision the opportunity to participate in debates on important issues in their local area. Another factor in favour of disclosure is that the public and those affected by decisions should be entitled to see the basis on which decisions are reached.

Weighed against this is the fact that the exempt appendix contains the observations and opinions of an external consultant about the expected and actual performance of investment managers. It also contains details of the investment processes/strategies of the investment managers.

It would not be in the public interest if advisors and officers could not express in confidence opinions which are held in good faith and on the basis of the best information available. The information to be discussed is also commercially sensitive and if disclosed could prejudice the commercial interest's of the investment managers.

It is also important that the Committee should be able to retain some degree of private thinking space while decisions are being made, in order to discuss openly and frankly the issues under discussion in order to make a decision which is in the best interests of the Fund's stakeholders.

The Council considers that the public interest has been served by the fact that a significant amount of information regarding the outcome of the report has been made available on these issues – by way of the main report.

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Document is Restricted

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Review of Hedge Fund Managers: Appendix 2

Signet

Mandate	Fixed income fund of hedge funds
Inception date & initial investment	31 July 2007; £45.3m
Current mandate size (30 Sept 2010)	£46.3m
% of Fund	c. 1.9%
Performance target	LIBOR + 3% p.a.
Fees	See JLT Report

Signet specialise in global fixed income funds and invest in underlying managers deploying a range of fixed-income related strategies including investment-grade government and corporate bonds, high-yield bonds, Emerging Market debt and distressed securities. Like Gottex, the Signet mandate is expected to have lower risk / return characteristics than the Man and Lyster Watson portfolios.

1. Organisation

Established in 1993, Signet's principal investment focus is on funds of hedge funds. Signet's client base is primarily institutional with approximately 95% of assets managed on behalf of financial and other institutions; the remainder consists of family offices and other qualifying investors. Signet have around £1.3bn assets under management in their Fund of Hedge Funds. Signet is independent and owned by its management and founders. Signet have one of the smaller teams of the Fund's FoHF providers, with a team of 16.

The majority of Signet's funds of hedge funds are listed either on the Irish Stock Exchange or the Luxembourg Stock Exchange. Signet Capital Management Limited is part of the Signet group of companies (Signet). Signet Capital Management Limited, authorised and regulated by the FSA and based in London, is the group's investment management company & distributor. Signet Capital Management Limited is advised by Signet Research & Advisory SA, located in Lausanne, Switzerland, and is the focus for manager research, due diligence, risk management and portfolio construction.

2. Structure and Key Facts

The Fund's investments with Signet are in their Global Fixed Income Fund, which invests in a portfolio of c.60 underlying managers diversified across a variety of fixed income strategies – this means they only invest in managers who invest in debt type assets and therefore do not invest in equities or commodities. Signet's Global Fixed Income Fund invests approximately 50% in credit and 50% in macro fixed income strategies.

Redemption terms are quarterly with 90 days notice.

The Fund is domiciled in the British Virgin Islands, and Signet Capital Management Limited is authorised and regulated by the UK Financial Services Authority.

3. Philosophy & Process

Signet's approach looks to generate superior investment returns within the parameters of capital preservation and systematic risk control. The investment process adopts a four-fold approach that combines "top down" strategy allocation and "bottom-up" manager selection, utilising a systematic approach to portfolio construction.

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Review of Hedge Fund Managers: Appendix 3

Stenham

Mandate	Multi Strategy fund of hedge funds
Inception date & initial investment	31 July 2007; £11.3m
Current mandate size (30 Sept 2010)	£11.4m
% of Fund	c. 0.5%
Performance target	LIBOR + 3% p.a.
Fees	See JLT report

Capital preservation is at the heart of Stenham's ethos. Stenham (along with Signet) have the lowest performance target of the Fund's FoHF managers. Stenham manage 5% of the Fund's allocation to Hedge Funds.

1. Organisation

The Stenham Group was founded in 1901. They have a 21 year track record in asset management and currently manage c. £2.2bn of assets. Stenham Asset Management is focused exclusively on alternative investment products, including multi-manager hedge fund portfolios and property funds. They focus on protecting the downside which forms an important part of the culture of the firm. Stenham's roots are in managing wealth of private families and they have grown into also managing assets for pension funds. Stenham is owned 51% by Peregrine Group (a South African financial services group) and 49% by management, all shareholders are also co-investors.

2. Structure and Key Facts

The Fund's investments with Stenham in their sterling denominated Universal II Fund, a relatively low volatility, liquid, multi-strategy portfolio. The Fund's portfolio is invested across c. 35 underlying managers.

Redemption terms are monthly with 95 days notice.

The Fund is registered in the British Virgin Islands.

3. Philosophy & Process

Stenham's investment style is conservative with a focus on capital preservation and minimising downside risk. They seek to achieve consistent absolute returns with low volatility through a combination of active strategy allocation and skilful manager selection. The portfolios invest in a range of assets, capital instruments, markets and strategies, which capture major market movements through the skills of the individual third party managers. They focus on avoiding extreme loss while finding managers that deliver alpha. Risk is limited through worldwide diversification and hedged strategies. Emphasis is placed on researching, monitoring and reviewing managers. The assets are allocated among arbitrage, equity hedged and global macro managers.

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Review of Hedge Fund Managers: Appendix 4

Lyster Watson

Mandate	Multi Strategy fund of hedge funds
Inception date & initial investment	31 July 2007; £9.5m
Current mandate size (30 Sept 2010)	£9.8m
% of Fund	c. 0.4%
Performance target	LIBOR + 4% p.a.
Fees	See JLT report

Lyster Watson have a higher return target than the lower volatility Gottex, Signet and Stenham funds, but a lower target than Man.

1. Organisation

Lyster Watson is a US-based, privately owned, investment advisory firm founded in 1992. They have been researching hedge funds for 18 years and managed fund of hedge funds for 11 years. As of the 30 September 2010, the firm's FoF assets under management were approximately £650m. Their clients include pension plans for corporations, unions and public plans, and endowments, foundations.

2. Structure and Key Facts

The Fund invests in their Moderate Volatility Fund, which is a multi-strategy portfolio with the scope to move across strategies. It is a US dollar share class (the Fund hedges the currency risk separately). The Fund's portfolio is invested across c. 30 underlying managers.

Redemption terms are quarterly with 60 days notice.

The Fund is registered in the Cayman Islands, and as a Registered Investment Advisor, Lyster Watson & Company is regulated by the U.S. Securities and Exchange Commission.

3. Philosophy & Process

Portfolios are constructed through diversification on a risk factors basis and not simply by underlying hedge fund strategies, looking to limit market exposures such as equity and interest rate risks. The committee determines strategy allocation targets at year-end; this top-down process sets targets which reflect the assessment of underlying factors and their impact upon the relative attractiveness of each hedge fund strategy. The hedge fund selection process is bottom-up. Once a fund has met the initial selection criteria, it qualifies for in-depth due diligence, where the fund's quantitative, qualitative and operational aspects are assessed. Approved funds are added to the Focus List, which are then considered for selection on a risk/return and liquidity basis by the committee. Funds are added with an aim of achieving low correlation to other funds within its strategy and to the portfolio as a whole.

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Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND INVESTMENT PANEL	
MEETING DATE:	12 JANUARY 2011	AGENDA ITEM NUMBER
TITLE:	PROPOSAL FOR SRI POLICY REVIEW	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
List of Attachments: Nil		

1 THE ISSUE

- 1.1 The Committee has agreed to review the Fund's policy towards Socially Responsible Investing (SRI) during 2011. This report sets out the proposed brief for the review and the Panel is asked to review the brief, make amendments and agree the final brief to recommend to the Committee.
- 1.2 It is envisaged that the SRI policy will be reviewed by the full Committee after the new Committee is confirmed following the May 2011 local elections. The review will be in two stages, the first to understand the background to SRI and agree an overall policy direction and the second to start developing an implementation strategy whilst recognising the impact/constraints of our existing investment strategy.

2 RECOMMENDATION

- 2.1 **The Investment Panel agrees any amendments to the brief for recommendation to the Committee.**

3 FINANCIAL IMPLICATIONS

3.1 The budget provides for investment advice to review the SRI policy.

4 BACKGROUND

4.1 The Investment Panel considered the Fund’s approach to SRI and corporate governance during 2010. However, given that SRI or ESG (Environmental, Social and Governance) and corporate governance covers a wide range of issues and there are a number of approaches to investing to be considered, it was agreed that it should be considered in full by the Committee in order to agree the Fund’s policy and direction of travel.

4.2 In the meantime a number of initiatives recommended by the Panel were approved by the Committee as follows:

- (1) To appoint a voting agent to monitor the Fund’s voting activity. This will improve transparency to the Committee and scheme members and strengthen the Fund’s compliance with the UK Stewardship Code and Myners Principles. Manifest were appointed in December as the Fund’s vote monitoring agent
- (2) To report the activity of the Local Authority Pension Fund Forum to the Committee on a quarterly basis.
- (3) To include an evaluation of the integration of environmental, social and governance risks within the manager’s investment process in all active equity mandate tenders. This was included in the global equity tender undertaken in 2010.

5 PROPOSED BRIEF OF THE REVIEW

5.1 The proposed review is set out below. The project has been divided into two Committee workshops which will enable work to be developed once objectives and direction of travel agreed following the first workshop. It is proposed that the first workshop will be held in July 2011. Papers will be prepared ahead of the workshop to provide information.

First workshop

Overview & Direction of Policy		
1	Overview of SRI/ESG investing	<ul style="list-style-type: none"> • How investment approaches to SRI/ESG/corporate governance have evolved • How UK regulations are influencing behaviour of UK plc <ul style="list-style-type: none"> - Examples of good/poor practice of UK plc • Investment/Regulatory framework <ul style="list-style-type: none"> - Ethical debate versus legal framework – including responsibilities of trustees - UK versus overseas equities - Stewardship codes & compliance regime - UN PRI – what it would mean for us to comply

2	Policy Development	<ul style="list-style-type: none"> • Preferred v Deliverable policy • Conflict of interest • Conflict of objectives • Timescales
3	Define Fund's objectives	<ul style="list-style-type: none"> • Define high level objective as to the Fund's role as a responsible investor and set realistic long term targets (direction of travel)

Second workshop

Implementation of direction of travel		
1	Recap of the Fund's current policy	<ul style="list-style-type: none"> • UK SRI equity portfolio • UK Stewardship Code compliance and voting policy • Manager selection process • Limitations of current investment structure – pooled funds, overseas assets
2	Does the Fund's current approach meet its objectives?	<ul style="list-style-type: none"> • Voting policy • Jupiter portfolio • Other portfolios
3	Implementation Assessment & options	<ul style="list-style-type: none"> • Policy impact assessment • Overlays • Specialist mandates (ranging from “screened” to “sustainability” portfolios) • Activism / voting policy
6	Action points	<ul style="list-style-type: none"> • Agree direction of travel and action points

5.2 The Panel are asked to discuss and agree the brief to be recommended to the Committee.

5.3 In addition, the Panel is asked to comment on whether holding the first workshop in July is appropriate given the first committee meeting post 2011 elections will only be on 24 June.

6 RISK MANAGEMENT

6.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further

strengthens the governance of investment matters and contributes to reduced risk in these areas.

7 EQUALITIES

7.1 An equalities impact assessment is not necessary.

8 CONSULTATION

8.1 N/a

9 ISSUES TO CONSIDER IN REACHING THE DECISION

9.1 No decisions are being made. The issues being considered to make a recommendation to the committee are contained in the report and comments are sought in the report.

10 ADVICE SOUGHT

10.1 The Council's Monitoring Officer (Council Solicitor) and Section 151 Officer (Divisional Director - Finance) have had the opportunity to input to this report and have cleared it for publication.

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Background papers	
Please contact the report author if you need to access this report in an alternative format	