BATH AND NORTH EAST SOMERSET COUNCIL

AVON PENSION FUND COMMITTEE

INVESTMENT PANEL

DRAFT MINUTES OF THE MEETING OF 27TH MAY 2010

Present: Cllr Gabriel Batt, Cllr David Bellotti, Ann Berresford, Cllr Mary Blatchford, Andy Riggs, Cllr Gordon Wood

Also in attendance: Tony Bartlett (Head of Business, Finance and Pensions), Tony Earnshaw (Independent Investments Advisor), Liz Feinstein (Investments Manager), David Lyons (Divisional Director, JLT Benefit Solutions)

1 EMERGENCY EVACUATION PROCEDURE

The Clerk read out the procedure.

2 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

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

3 DECLARATIONS OF INTEREST

There were none.

4 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIRMAN

There was none.

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

There were none.

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

A Member asked about the Fund's exposure to BP in the light of their current environmental problems. The Investments Manager said that the Fund held a large holding within the passive portfolio. She would email the details of the holding to Members the following week.

7 MINUTES: 25TH FEBRUARY 2010

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

8 CURRENCY HEDGING

The Investments Manager presented the report. She said that it summarized all the work that had been done by the Panel in this area to date. It was proposed to actively hedge US Dollar, Euro and Yen denominated equities and to appoint a non-discretionary currency manager to implement this.

A Member asked about the size of the pool of suitable managers. The Investments Manager thought there would be about eight. The mandate would be tightly specified, to eliminate those practising active currency <u>management</u> rather than hedging. Mr Lyons said that five had been identified at the time of the original definition, though and additional one or two might have entered this field since.

A Member asked what the effect on the Fund would have been of implementing active currency hedging over the past twelve months. The Investments Manager replied that hedging would only be implemented when it was favourable to the Fund to do so. As sterling had been weakening there would have been no need to hedge against currency exposure. Hedging was more costly when there were frequent small movements in sterling so that the hedge would be put on and taken off more frequently. It was more profitable to implement hedging when there was a trend in relative currency values. The Member said that he was concerned that hedging required the manager to make judgments about future currency values and that this involved risk. Had the crisis in Greece or the weakening of the Euro been predicted? Mr Lyons responded that active currency hedging could be implemented in a purely mechanistic way, and that over the past twelve months there would have been no hedging of the US Dollar or the Yen, because sterling had been weakening against these currencies. The Independent Investment Adviser said active hedging could be practised without the need to make judgements, through the use of triggers. The Investments Manager explained that the trigger could be the relationship between the current rate of the foreign exchange and its future anticipated rate at that point in time which would create a projected trend line; a hedge would be put on, or removed, if the current rate rose above, or fell below, the trend line. This eliminated the need for judgment in the process.

It was agreed that Members should be involved in the appointment of the manager for the mandate. It was agreed that a special meeting of the Panel should be convened and that Panel Members able to attend that meeting would be involved in the selection of the manager but that the process should be delegated to officers.

RESOLVED to recommend to the Avon Pension Fund Committee:

(i) to appoint a specialist manager to implement an active currency hedging mandate over all US Dollar, Euro and Yen denominated equity assets (excluding those in emerging markets);

(ii) to agree that the manager to be appointed a non-discretionary quantitative approach to active currency hedging;

(iii) agree to delegate the appointment process to Officers in consultation with the Chair of the Committee and Members of the Investment Panel.

9 GLOBAL EQUITY – TENDER PROCESS

The Investments Manager presented the report. The appointment of a global equity manager had been agreed at the last meeting of the full Committee; the report set out the tender process for this appointment. She invited Members to comment on the two options for the selection meeting given in paragraph 4.5 of the report.

A Member asked whether there could be a two-stage process, with the Panel making a recommendation to the full Committee, which would take the final decision. The Investments Manager was concerned that this would cause significant delay in making the appointment.

After discussion it was **RESOLVED** that the Investment Panel would recommend to the Avon Pension Fund Committee to agree the proposed tender process for the Global Equity Tender as set out in 4.3 and that the selection meeting should be constituted as a special meeting of the Investment Panel with authority to appoint (which would be open to other Members of the Avon Pension Fund Committee who wished to attend).

10 REVIEW OF INVESTMENT PERFORMANCE FOR QUARTER ENDING 31 MARCH 2010

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 item 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.

The Investments Manager presented the report. She explained that because of the timing of today's meeting the report was less detailed than the report to be presented to the next meeting of the full Committee. She noted that during the period the policy decision to change the allocation of 60:40 UK: Overseas equities to 45:55 had been implemented. Also the tactical position overweight corporate bonds/underweight gilts had been reversed in January when the reversal point was triggered, realising a net benefit of £4.2m. She drew attention to the information in paragraph 4.8 of the report, relating to the underperformance of the Fund relative to the average fund in the WM Local Authority Fund universe.

The Head of Business, Finance and Pensions drew attention to paragraph 5.2 of the report which stated that two policy issues would be placed on future agendas of the policy, namely (1) the level of assets managed by one manager; (2) the allocation to emerging markets.

A Member noted that there was a widening gap between the rolling three-year return and the rolling three-year benchmark return shown in the graph on page 14 of the JLT review. The Investments Manager replied that the widening of the gap in 2008-09 was due to the particularly poor performance of hedge funds against their cash based benchmarks.

A Member noted the poor return on the cash holdings of the Fund, as reported on page 15 of the review. She wondered whether some of this could be invested in property. The Investments Manager said that a balance had to be struck between having sufficient liquidity ready to invest in property and maximising returns. Equities managed by BlackRock had been sold when the equity market had rallied, and the aim was to maintain 25% of the assets earmarked for property in cash. The Independent Investment Adviser noted that Partners had managed a property portfolio for the Fund for almost a year, yet there was no commentary about them. Mr Lyons replied that there was information about the Fund's investment in property on page 16 of the review. The Investments Manager said that qualitative information, about Schroders and Partners would be included in the September performance report; however, quantitative data would not be particularly insightful at this early stage of investing.

A Member was pleased to note that statement on page 19 of the review that *"the total Fund has benefited from diversification by asset classes, as Fund volatility is lower* *than the equity managers and the BlackRock multi-asset portfolio, despite these making up a large proportion of the total assets."*

A Member wondered whether the performance of BlackRock, as reported on page 32 of the review, should be a cause of concern, in that their return was considerably in excess of expectations. This made her worry whether they were taking excessive risks. The Investments Manager said that this was because the tactical switch of equities v. bonds and the UK:Overseas rebalancing had been done through them. In addition, surplus cash had been invested through them.

The Chair asked how the markets were reacting to the Government's attempts to reduce the UK budget deficit. Mr Lyons said that the cuts announced so far had been favourably regarded, but global events, such as the situation in Greece and the decline in the Euro, were the major preoccupations.

A Member asked about the performance of the Fund relative to other local authority Funds. The Investments Manager said that over the year the Fund had lagged against the average of funds in the WM universe. This was because relative to other funds the Fund was underexposed in equities and slightly overweight in bonds and hedge funds. Over a three-year period, however, the Fund was ahead of the WM universe aided by the diversification out of equities. However, annual performance comparisons were becoming more difficult because the Funds in the WM universe have adopted increasingly diverse asset allocation strategies.

RESOLVED to note the Fund's return on investments and details of manager performance as set out in the report.

The meeting returned to open session.

11 HEDGE FUND REVIEW – BRIEF

The Investments Manager presented the report. She said that she thought it was important for the full Committee to be involved in the review because it was a strategic issue.

A Member said that there was a great deal of activity worldwide on the regulation of hedge funds. He believed that the Committee should receive a report on changes in regulation and potential implications to set the scene for the review. After some discussion it was agreed that it would be appropriate for the officers to commission an independent report on regulation from lawyers or other expert advisors to complement the information from the investment consultant and fund of hedge fund managers. It was agreed that the review of trends in regulation should be done in parallel with stage (2), the strategic review by the investment consultant.

RESOLVED to recommend the proposed brief to the Avon Pension Fund Committee, with the addition of a review of the emerging international regulatory environment to be done in parallel with the strategic review by the investment consultant.

12 PANEL WORKPLAN

The Investments Manager presented the report. She said that it might be difficult to have a meeting of the Panel in September and that she would be consulting Members about an alternative date. Meeting hedge fund managers was a priority.

A Member said that the Partners portfolio was a complicated one and that it would be helpful for Members to have a summary of the current state of play. The Investments Manager undertook to provide an overview.

RESOLVED to recommend the workplan to the Avon Pension Fund Committee.

13 ANY OTHER BUSINESS

The Chair thanked Members and Officers for their contributions during the Panel's first year. Nominations for membership for the next year would be taken at the next meeting of the full Committee.

The meeting finished at 3.10pm.

Chair……………………………………………….

Date confirmed and signed……………………….