LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE PENSIONS COMMITTEE

HELD AT 7.30 P.M. ON THURSDAY, 19 SEPTEMBER 2013

COMMITTEE ROOM C1, 1ST FLOOR, TOWN HALL, MULBERRY PLACE, LONDON E14 2BG

Members Present:

Councillor Zenith Rahman (Chair)
Councillor Judith Gardiner
Councillor Ann Jackson
Councillor Craig Aston

Admitted Bodies, Non-Voting Members Present:

Frank West - Non-Voting – Non-voting Member Representing Trade Unions
John Gray - Non-Voting – - Non-Voting Member (Admitted Body)

Others Present:

Raymond Haines (Chair of Pensions Fund Investment Panel)

Matt Woodman Hymans Robertson

Lynn Coventry WM - State Strret

Officers Present:

Anant Dodia – (Pensions Manager)
Chris Holme – (Acting Corporate Director - Resources)
Oladapo Shonola – (Chief Financial Strategy Officer, Resources)
Antonella Burgio – (Democratic Services)

COUNCILLOR ZENITH RAHMAN IN THE CHAIR

INTRODUCTIONS

The Chair welcome in Coventry of The WM Company who was in attendance to speak to the committee on the annual performance of the pension fund.

ORDER OF BUSINESS

To facilitate the discussion of the report, the Chair moved that the order of business be varied. The Committee approved the motion and accordingly Item 5.1 Annual Update from WM was taken as the first item of business. Following discussion of this item, the Chair moved that the order of business be resumed. The Committee approved and consideration of business resumed, as printed in the agenda, from item 1.

1. APOLOGIES FOR ABSENCE

No apologies for absence were received.

2. DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST

No declarations of disclosable pecuniary interests were made.

3. UNRESTRICTED MINUTES

The minutes of the meeting held on 25 June were approved as a correct record. The minutes of the meeting held on 25 June were approved, without amendment, as a correct record of proceedings.

4. DEPUTATIONS & PETITIONS

No requests to address the Committee without prior notice (deputations) or to present petitions were received by the Chair

5. UNRESTRICTED REPORTS FOR CONSIDERATION

5.1 Annual Update from W M

Ms Coventry of The WM Company tabled the report "London Borough of Tower Hamlets performance review period ending 31 March 2013." She introduced herself and advised that The WM Company tracked the performance of 90% of local authority pension funds. She advised that her presentation would comprise the following elements:

- financial returns, strategies and trends
- the annual performance of Tower Hamlets pension fund,
- the performance of Tower Hamlets pension fund compared with other local authorities

Financial returns, strategies and trends:
Ms Coventry advised that returns on equities in the period 2012 – 13 had been favourable. Active managers had done well against benchmark and there had been above index return in all markets except USA. She advised that equities performance had been volatile (page 5) but returns were above average over 3, 5, 10 and 20 years. Performance of bonds had been less volatile but returns were lower especially over 10 and 20 years.

She advised that:

- annual returns in respect of alternatives (page 6) were 9.2% over 20 years but this did not apply to all categories of alternatives
- average returns in both cash and alternatives categories were below equities

- annual returns for property were in line with quoted levels but presently still negative
- average total assets returns for local authorities had achieved benchmark

Therefore returns had been achieved but liabilities were higher.

Asset allocation performance (page 8) tended towards reducing risks and, to achieve this, portfolios were more diversified. As funds were restructuring there was a move towards global markets; UK equities comprising 30% and the remainder comprised of overseas equities. Mr Woodman enquired and Ms Coventry confirmed that Investec were an absolute return category of fund. She noted that the Council's decision to invest in these funds was ahead of trend.

The Chart ‘Performance Range Relative to Benchmark’ (page 9) indicated the performance range over 1, 3, 5 and 10 years compared to its own benchmarks. Ms Coventry advised that most returns had exceeded their benchmark and that some benchmarks are being measured against cash which had rendered it easier to outperform benchmark. However, most 5-year investments had underperformed. Mr Gray enquired and Ms Coventry confirmed that the performance reported was gross of fees.

Annual performance of Tower Hamlets pension fund:
Ms Coventry provided the following information in relation to total fund performance against strategic benchmark:

- The total Fund value summary (page 11) indicated the fund composition across the fund managers and was valued at £929 million at 29 March 2013, 63% of this was allocated to equities.
- Relative fund returns (page 12) were 11.8% in 2013; these were ahead of benchmark within the year. Performance over 20 years was 0.5% below the benchmark. This low return was due to exposure to UK equities.
- Mr Shonola advised that manager, Martin Currie and Aberdeen Asset Management had been dismissed two years ago and the Fund moved to a passive mandate for UK equities.
- The Fund had underperformed over the last five years, however other local authorities funds had performed similarly
- Tower Hamlets’ performance was in the middle of the range compared to other authorities with lower risk and with lower risk than other authorities. It was noted that the lower risk was due to the fund structure which contained passive strategies.

Ms Coventry provided the following information concerning manager performance (section 3):

- Tower Hamlets fund was 0.6% ahead of benchmark and the following manager performance was noted:
    - GMO performance was below the benchmark
    - Legal and General was a passive manager and matched benchmark as expected
    - Baillie Gifford had delivered good returns above benchmark

Performance of Tower Hamlets pension fund compared with other local authorities:
Ms Coventry provided the following information (section 4):

- the Fund had outperformed against its own strategy. It was noted that this would drive performance more than managers performance
- comparison with other local authorities' performance needed recognise that each of them operated different funding strategies. Mr Shonola noted that the Tower Hamlets strategy reflected its present position and its strategic aims
- in the last year and in the longer term Tower Hamlets was 1.8% below average. Asset allocation only added 1% therefore stock selection was the driver
- Bonds return was 4.9% below the local authority average
- in regard to the absolute risk and return percentage over 5 years (page 20), Tower Hamlets' performance was in the lower range of risk and therefore average performance could be expected
- the latest five-year risk and return chart (page 21) also indicated Tower Hamlets fund position in the lower risk return range
- many other authorities were presently engaging a larger number of managers to deal with their investments

Due to time constraints the Chair moved and the Committee agreed to submit written questions concerning the presentation to Ms Coventry.

Ms Coventry left the meeting; the Committee then discussed the presentation and the following matters were raised:

- Cllr Jackson noted that the strategy, while conservative, was not totally risk averse. The Committee was advised that:
    - that the Fund had performed within the local authorities' cluster.
    - the Council had taken a decision against exposure to a lot of risk
    - two years ago a decision had been taken to invest UK equities via a passive mandate.
    - the strategy was the driver of performance rather than the managers engaged
- Cllr Gardner enquired whether benchmarks were sufficiently ambitious within their own categories and whether it may be necessary to change the strategy in order to benefit from greater returns. The Committee was advised that:
    - as the benchmark level indicated the level of exposure of the investment, if risk were higher the benchmark would be also higher correspondingly.
    - Mr Woodman noted that equity markets, since the financial crisis of 2008, had been supported by quantitative easing by the United States Federal reserve and therefore did not recommend that more equity exposure was undertaken at the this time
    - Mr Haynes noted that active equity managers in the UK had not outperformed the market for a long period.

- Mr Holme suggested that small improvements to the strategy should be considered after the triennial evaluation. It was noted that the funding strategy statement (triennial evaluation) would be available at the end of 2013 and brought to committee in February 2014.

- Cllr Jackson enquired why less complex funds had produced high returns. She was advised that Hymans Robertson had studied this matter and the returns were due to:
  - high levels of diversification which enabled such funds to weather any unfavourable markets and
  - low manager turnover because this action involved costs

  In view of this, Mr Woodman recommended that unnecessary changes to fund structure should be avoided.

- Mr Gray enquired:
  - what cumulative performance would be given if figures were reported net of fees. Mr Woodman illustrated his answer referring to 'total assets' at page 7 of the presentation and advised that total assets reported over 10 years were 9.4, equivalent to a 90% return over the period. This figure was a gross sum and 3% should be removed for fees over the annual period.
  - how net figures could be better reported and Mr Shonola advised that it would be difficult to persuade managers to report these figures since fee structures would likely be disclosed; this contractual information was confidential. Additionally fees were in fact paid at different times and at different rates; therefore for reporting purposes, sums were annualised. He noted that the table also gave indicative costs of running the fund.
- Mr Gray noted that it would be beneficial to quantify fees as they amounted to a sizeable sum when compounded over 10 years. Mr Woodman supported the principle of reporting performance net of fees but felt that WM would not be able to provide these figures as managers' fees would then be disclosed and this was commercially sensitive information.

RESOLVED:

1. That the tabled report and the verbal update be noted
2. That the Committee's question be submitted to Ms Coventry in writing

Action by:
Oladapo Shonola, Chief Financial Strategy Officer – Resources

5.2 2012/13 Local Government Pension Fund Annual Report

Mr Shonola presented the report circulated at agenda item 5.2 which gave an overview of activity of the scheme and of the fund over the year and stated that the report was for noting only. He advised that the auditors have given an unqualified opinion of the accounts following the audit of the statement of accounts.

Referring to paragraph 6.3 the report, he advised that the fund was presently cash flow positive and it was estimated that the fund would become cash flow negative in a two-year range, dependent all the numbers joining and leaving the scheme.

The following issues were discussed:

Impact of auto-enrolment regulations on Pension Scheme membership -
Mr Holme advised it was too early to quantify the effects; however a significant number of staff that were auto-enrolled have already opted out. Mr Dodia suggested that present economic hardships may have led lower paid employees choosing to opt out of the scheme as contributions had a significant impact on available cash in households where income was low. It had been noted also that some members had opted out almost immediately and this had influenced some other longer-term members to opt out also. However the Council still promoted enrolment. Mr Holme advised that a three months analysis would be undertaken to investigate un-enrolment.

Cause of differential performance:
Councillor Jackson noted that the Fund had made better than average returns over 20 years but returns had been less favourable in the latter 10 years, and enquired what had caused the better performance in the earlier part of the period. Mr Woodman advised that equities always outperformed bonds over 20 years; however the differential performance had arisen because equities were very strong in the first part of the 20-year period but weak over the latter part.

RESOLVED:

That the report be noted

5.3 Report of Investment Panel for Quarter Ending 31 March 2013

Mr Shonola presented the report at item 5.3 which informed the Committee of Fund performance in the 4th quarter 2012 – 13.
He advised that:

- equities performance was strong
- seven of the eight managers had outperformed their benchmarks
- GMO had had a good return but had not performed outperformed benchmark
- asset allocation was in line with the funding strategy
- many of the data and matters reported had been discussed by the Committee at agenda item 5.1

Mr Gray noted that the figures at page 28 and 29 of the agenda did not match and was advised by Mr Shonola that the statement of accounting was that of the last actuarial evaluation. Since that time, more bodies had been admitted to the Fund and hence the difference in the figures reported.

RESOLVED:

That the report be noted

5.4 General Update on Emerging and Developing Pension Fund Issues

Mr Shonola presented the report circulated as agenda item 5.4 which advised the Committee of emerging issues affecting the pension fund. He advised that, further to the findings of the Hutton commission on public sector pensions, the Government enacted new legislation to impose changes on Local Government pension schemes. These proposals (Local Government Pension Scheme 2014) were given at paragraph 6 of the report. The following points were also noted:

- Accrued rights would be protected
- A pensions board would be established, although guidance was still awaited on this
- conflicts of powers
- Complaints from academies that contribution rates were too high and the guarantee including caveats offered by the government
- The more admitted bodies admitted into the scheme escalates the risks of failing academies to which the fund might be exposed

In response to Members' questions the following information was provided

Concerning the Academy's pension fund deficit guarantee councillor Gardner stated that the Council should endorse its current approach to admitted bodies because of the level of risk being taken on.

Concerning a likely publication date of Government guidance relating to the powers and constitution of local government pensions boards, the Committee was advised no date had yet been indicated.

Councillor Gardner noted that the administration of an independent board or panel would add costs to the pension fund and suggested that a combined pension body approach would be a preferred option.

Concerning the degree of Fund exposure to bankruptcy risks, Mr Shonola advised that were several admitted bodies to become insolvent, the risks of failure would be borne by the remaining solvent bodies and ultimately by the Council therefore the risk to the Council was the greater. It was noted that these risks related to non-teaching staff as teachers' pensions were covered by other schemes.

Noting the proposed transition to an average contribution arrangement and higher contribution levels, Councillor Jackson argued that these had contributed to the higher opt out rate and suggested that in future the fund will find it more difficult to generate income because the Fund cash or value base would be degraded. Mr Holme advised that the forthcoming actuarial assessment would consider this matter and to counteract decline it was necessary to continue to promote the Fund. Mr Woodman noted that because the accrual rate would be higher, conditions would remain consistent in the main.

Mr Gray noted that, compared to other pension schemes available, local authority schemes still offered better benefits to low paid and part-time workers and was advised that the contribution rate was variable depending on the earnings of each member of the fund.

Concerning future fund structure, Mr Shonola advised that there might be a Government call for merger to form a super fund. In view of this the London Councils undertook a survey of interest in the possibility of setting up a common investment vehicle that would enable London boroughs to pool assets while retaining local accountability. Mr Holme advised that, on the whole, London boroughs were not in favour of pension funds mergers and were working together to investigate the possible advantages of a common investment vehicle.

Councillor Aston requested a report on how the Hutton proposals would work and possible options to address issues around governance and powers, duplication. Mr Holme advised that an update would be provided at the next committee a report would presented once Government guidance had been issued.

RESOLVED:

1. That the report noted
2. That an update on how the Hutton proposals would work and possible options to address issues around governance and powers, duplication be provided at the next committee and a report presented once Government guidance had been issued.

Action by:
Oladapo Shonola, Chief Financial Strategy Officer – Resources

6. TRAINING EVENTS

The following general matters were discussed:

- where possible, training events delivered free of charge should be exploited to avoid costs other than necessary. Noting this recommendation, Mr Shonola advised that the UBS courses notified at 6.2 and 6.3 were free of charge and suitable for members recently appointed to the Committee.

- possible solutions to maximise training including:
  - mandatory requirement to attend training on appointment to the committee
  - bespoke training,
  - incorporating training into the first half hour of each committee

- use of the on-line pensions regulator trustee training package

Mr Haynes noted that:

- should regulations be changed, training would need to be given greater consideration
- managers were often willing to provide short training for members

6.1 LGPS 2100 Training and Investment Seminar

The training information was noted and Members who wished to attend were asked to contact the clerk to the Committee.

6.2 Introduction to Investments for Trustees

The training information was noted and Members who wished to attend were asked to contact the clerk to the Committee.

6.3 Investing to meet your liabilities

The training information was noted and Members who wished to attend were asked to contact the clerk to the Committee.

6.4 Local Authorities Pension Fund Forum Annual Conference

The training information was noted and Members who wished to attend were asked to contact the clerk to the Committee.

6.5 London Borough of Merton – Learning and Development Agenda

The training information was noted and Members who wished to attend were asked to contact the clerk to the Committee.

Action by:
Antonella Burgio, Democatic Services Officer – Chief Exec's

7. ANY OTHER UNRESTRICTED BUSINESS CONSIDERED TO BE URGENT

Nil items.

The meeting ended at 9.03 p.m.

Chair, Councillor Zenith Rahman
Pensions Committee