PAPER A

Minutes

Name of meeting	**ISLE OF WIGHT PENSION FUND COMMITTEE**
Date and time	**13 JULY 2012, 10.00 AM**
Venue	**COUNCIL CHAMBER, COUNTY HALL, NEWPORT, ISLE OF WIGHT**
Present	Councillors: Peter Bingham (Chairman), Barry Abraham, Reg Barry, Ian Ward, Wayne Whittle, Ian Stephens and Stuart Hutchinson Admitted Bodies: Stephen Lamdin, Isle of Wight College and Theresa Dunford, Cowes Harbour Commission Representatives: Chris Lisher, Admitted Bodies Representative Steve Milford, Unison Representative Officers: Dave Burbage, Strategic Director of Resources, Jo Thistlewood, Technical Manager and Carol Harrison – Minutes.
Apologies	Councillor: Vanessa Churchman

RECORDING

10. **Minutes**

Members reviewed the minutes of the previous meeting held on 18th May 2012.

RESOLVED :

THAT the minutes be agreed as a correct record.

11. **Declarations of Interest**

Cllr Reg Barry and Cllr Wayne Whittle declared an interest as a member of the Isle of Wight Pension Fund and in receipt of an Isle of Wight Council Pension.

12. **Public Question Time**

No members of the public were present

13. **Welcome by Chairman of the Committee**

The Chairman Cllr Bingham welcomed everyone to the annual meeting and presented the annual report of the Pension Fund Committee for 2011/12.

The overall Fund value at 31st March 2012 was £334.8m up from £326.5m as at 31st March 2011.

Performance in 2011/12 had been mixed against a backdrop of continued volatility and uncertainty in the Eurozone. The overall fund performance was a return of 2.7%. The WM League Tables for some 100 Local Authority Pension Funds put the Isle of Wight Council Fund in overall 72nd place compared to 8th the previous year. For UK Equities 32nd, UK Bonds 60th and property 7th. The overall performance was particularly disappointing in global equities where the Fund was 96th and this dragged down the overall performance.

The three Investment Managers would be attending today's meeting to give an overview of their performance and the key issues involved.

As always with performance we need to take a longer term view and in August this year we would have had our current investment structure and managers for 3 years and we will be undertaking a review of overall performance and asset allocation later in the year.

During 2011/12 we tendered our actuarial services and investment advisory services and from 1st April 2012 Hymans Robertson have been reappointed to deliver actuarial services to the Fund and Mercer's have been appointed to deliver our investment advisory services. The Chairman introduced Jo Holden from Mercers who will be attending the Committee meetings in the advisory role.

The annual report of accounts for 2011/2012 is on the agenda and it sets out the overall financial activity and statements of the Pension fund. This also includes the Funding Strategy Statement, Statement of Investment Principles and the Governance Compliance Statement that have all been reviewed by the Committee.

As reported previously the Local Government Pension Scheme is being reviewed and the latest proposals for changes to be introduced for 1st April 2014 are also reported on.

Reports of the Strategic Director of Resources

14. **Report of the Annual Pension Fund Accounts (Paper B)**

The Technical Finance Officer presented the draft annual report and accounts for the Isle of Wight Pension Fund for the year ended 31st March 2012. The accounts contained within the annual report will form part of the Isle of Wight Council's accounts for the year ended 31st March 2012. They were presented to the Audit Committee in draft on the 28th June 2012 and final approval will be made in September 2012. These accounts are subject to audit.

The most significant changes in presentation of the accounts in 2011-12 are:

a) The requirement to include comparative (prior year) figures for all the major notes to the accounts, not just the fund account and net assets statement. This has necessitated the inclusion of additional tables for membership numbers (note 1b) and movements in investments (note 17a)
b) More detailed disclosures concerning financial instruments including the identification and interpretation of risks relating to those instruments (notes 18 and 19).
c) Increased transparency in respect of related party transactions (note 26), including disclosures of committee members who are active members of the scheme or in receipt of pension benefits.

The statement of investment principles, funding strategy statement and governance compliance statement were considered at the Committee meeting on 18th May 2012. The amendments requested at the meeting on the 18th May have been incorporated into these statements, which are included in the Annual Report and Accounts as appendices C, D and E respectively.

The 2011-12 accounts show that the fund generated a surplus (net increase in the net assets available for benefits) in the year of £5.295 million. This compares to £32.809 million in the previous year.

The main reasons for the reduction in surplus are:

- An increase in the lump sum retirement benefits paid in the year as a result of the redundancy programme undertaken by the Council, including the school reorganisation project.
- A decline in the change in market value of investments in the year following the volatility of both UK and Global Equity markets throughout the year.

The audit of the pension fund accounts commenced in June 2012 and the Audit Commission expect to issue their report on the accounts before 30th September 2012, the statutory date for publication of the Council's audited statement of accounts. The independent report of the Audit Commission will be presented to the Audit Committee during September 2012.

RESOLVED:

> THAT Option 2 be agreed and that the draft annual report and accounts are approved for inclusion in the Council's statement of accounts following completion of the audit process.

15. **LGPS Update (Paper C)**

The Strategic Director of Resources updated the committee on the latest position on proposed changes to the Local Government Pension Scheme.

The latest discussions have been looking at a single solution to both short and long term issues with a view to having regulations in place by 30th March 2013 (so that scheme changes can be taken into account at the next three year revaluation) with implementation on 1st April 2014.

The principles and an outlined timetable were produced by the LGA and were detailed in the report. Following further discussions the Local Government Association (LGA) and trade unions announced on 31st May 2012 the outcome of their negotiations on new LGPS proposals to take effect from 1st April 2014. These will now form the basis of consultation with Employers and Unions.

RESOLVED:

THAT the Committee note the report.

16. **Admitted Bodies (Paper D)**

The Strategic Director of Resources presented his report which set out the latest position on the Council's Highways PFI contract process that will result in a new admitted body to the Fund.

Following a report to the last Committee (18th May 2012) regarding the transfer of Ventnor Botanic Gardens, the report also highlighted the likely areas of further transfers and in particular the Highways PFI.

The Council is finalising the procurement stage for Highways PFI and formal approval is sought to the inclusion of the selected provider as an admitted body to the Fund.

The final decision on the award of the contract will be taken at Full Council on 22nd August 2012 and the contract documentation including the admission agreement, will be signed thereafter.

In respect of the transfers being undertaken it has not been felt necessary to enter into Bonds with the new employers as the number of staff involved have been small and the key risks are met by the Council. The actuary when assessing the need for a bond does not assess the solvency or financial viability of the contractor but merely the extent of pension fund risk that the contractor is meeting. In this case the basis of the transfer is that the Council retains nearly all the risk with the contractor only meeting one-off additional costs of early retirements, redundancies and pay increases above the norm. The need for a Bond is therefore not justified. The Council as letting authority provides an indemnity as part of the admission agreement so that the fund and other employers in the scheme are protected.

RESOLVED:

THAT recommendation 1 is agreed for the inclusion of the Highways PFI contractor if agreed by Full Council on 22nd August 2012, as an admitted body to the fund as from 1st April 2013 on the basis of an admission agreement (signed on or around the 29th August 2012) agreed by the Strategic Director of Resources that protects the fund from any additional liabilities.

17. **Pension Fund Risk Report (Paper E)**

The risk report was noted.

18. **Performance Review 2011/12 – Fund Managers**

Newton attendees: Jeff Munroe (Investment Manager); David Moylett (Account Manager)

Mandate: Aim to outperform MSCI All Countries World Index by 2% per annum over rolling 5 year periods.
Current value: £107.5m as at 9 July 2012
Performance to 30 June 2012: 6 months (Fund +7.30% versus benchmark +4.70%); 1 year (Fund -5.43% versus benchmark -4.28%); since inception on 28/08/2009 (Fund +8.90%pa versus +8.30%pa).

Summary of presentation:

The Newton delegates began by introducing themselves and explaining their respective roles. Jeff Munroe, Head of Global Equities, relinquished his role as Chief Investment Officer early in 2012 so that he could concentrate fully on delivering improved investment performance from Newton's global equity team. This meant that he personally took over the role of investment manager for the assets invested by the Isle of Wight Pension Fund. He acknowledged that this change followed a period of disappointing performance, particularly in the second half of 2011, during which time he and his colleagues at Newton believed that their relative performance should have been better. As head of the team, he has instigated a number of operational changes to strengthen the quality of the portfolio, including the requirement for greater regular stress-testing of all holdings. This has led to an improvement in relative performance in 2012 and Newton are confident that this will continue into the future.

The economic and market background over the last three years has been difficult for fundamental investors. The major challenge has been the fact that as and when developed world economies have shown signs of extreme distress - a regular occurrence over recent times - the authorities have been forced to embark upon a series of unconventional support mechanisms to support try to support the foundations. These interventions have generally given cyclical sectors of global stock markets a short term boost as investors have interpreted these interventions a being a cure for all ills. Unfortunately, the duration of these relief rallies has been getting ever shorter and there is now an acknowledgement that major reconstructive surgery is needed as opposed to regular doses of short term medicine.

Looking at Newton's performance, following a relatively disappointing second half of 2011, performance had been much stronger in 2012 since Jeff took over the management of the Fund. Stock selection had been good with particular highlights coming from the consumer staples and technology sectors. The biggest negative over the last six months was not holding Apple.

Looking forward, against what Newton believe will continue to be a challenging background, the focus of the portfolio continues to be on identifying stable growth companies as opposed to cyclical growth companies. Consequently, the portfolio remains overweight in healthcare, consumer staples and telecommunications companies. They have also identified a number of attractive opportunities in the technology sector. The largest underweight sectors are banks (where they continue to avoid western banks), industrials and consumer discretionary sectors where fortunes of many of the participating companies is likely to be correlated with the economic background.

The presentation concluded with Newton expressing their confidence that relative performance will be good over the longer term. They also flagged up that the balance between the requirement to reduce the unprecedented levels of global debt and the need to stimulate growth likely to generate further market volatility over the short and medium term.

Majedie Asset Management

Represented by Robert Harris and Simon Hazlitt, presented performance for their part of the Isle of Wight mandate to the end of March 2012. They have outperformed their benchmark, the FTSE All Share, by an average of 1.9% per year, since inception in August 2009.

The main positive contributors to the outperformance were the positions in large companies whose businesses are more resilient in the downturn. Also helpful was the decision to avoid most of the larger mining companies that have fallen sharply in the wake of weakening commodity prices. The main reason for the outperformance not being greater was the decision to avoid other “defensive” shares like Diageo and BAT, shares that Majedie consider expensive.

Whilst Majedie believe that the process of government and consumer “deleveraging” (paying down debt) will last for some considerable time and bear down on aggregate national GDP growth, there are some opportunities for the nimble investor, especially where general sentiment is too despondent and the shares are too cheap.

Schroders – UK Equities, Bond & property (Edward Chamberlayne and Jonathan Harris)

Edward Chamberlayne explained that Schroders managed three mandates for the Pension Fund. These consisted of a UK fixed income portfolio valued at £77.1m (at 31/3/12), a UK equity portfolio valued at £51.6m and a UK property portfolio valued at £19.8m. The sharp rise in risk aversion in the second half of 2011 as a result of rising concerns about the impact of the Eurozone sovereign debt crisis had resulted in strong returns from UK gilts (which are perceived as a safe asset) but relatively weak returns from UK equities. The UK bond portfolio returned 11.3% for the year, the UK equity portfolio -2.5% and the UK property portfolio 7.4%, being predominately rental income. Relative performance in fixed income and equities was disappointing over the year as the portfolios were not positioned for the sharp deterioration in the growth outlook precipitated by the Eurozone troubles. However, the longer term performance remains ahead of the benchmark.

Jonathan Harris gave a detailed review of the fixed income portfolio. Schroders considered that corporate bonds presented a more attractive investment opportunity than gilts. UK corporate bonds offered a yield of over 3% above that available on gilts which was very attractive by historic standards. Default rates were expected to remain low as companies had rebuilt their balance sheets over the last few years. A well-constructed portfolio of corporate bonds was likely to outperform gilts.

Edward Chamberlayne explained that the valuation of the UK equity market was low by historic standards. It was possible to purchase many good quality companies with dividend yields of over 6% and the prospect of growth in those dividends. Vodafone, AstraZeneca and Legal & General were three such examples. Although the short term outlook for the market remained uncertain, these companies were expected to produce good returns for investors over the medium term.

UK commercial property values had recovered sharply from their lows but had stabilised over the last year. The outlook is for flat to gently declining values with the return from property derived principally from rental income. The fund has focussed its attention on London and the south east where investor appetite remains keenest and has taken a cautious approach to the retail sector. With consumer spending expected to remain under pressure, high street retailers in particular are likely to find the trading environment tough resulting in downward pressure on property values.

Meeting closed at 13.00 pm

CHAIRMAN