

Agenda item:

Pensions Committee

On 17/09/09

Report Title. **Fund Performance update**

Report of **The Chief Financial Officer**

Signed :



Contact Officer : **Colin Duck – Corporate Finance**
Telephone 020 8489 3726

Wards(s) affected: **All**

Report for: Noting

1. Purpose of the report

- 1.1. To consider the latest investment performance data for the Pensions Fund and for each of the Fund's investment managers.
- 1.2. To compare responsible investments information provided by our Fund Managers with that supplied by LAPFF.
- 1.3. To report 2009/10 budget monitoring to the end of July 2009.

2. Introduction by Cabinet Member

2.1 Not applicable.

3. State link(s) with Council Plan Priorities and actions and /or other Strategies:

3.1. Not applicable.

4. Recommendations

- 4.1 That the Fund performance position as at end of June 2009 be noted.
- 4.2 That responsible investments information provided be noted.
- 4.3 That the budget management position to the end of July 2009 (period 4) be noted.

5. Reason for recommendations

- 5.1. This report is for noting.

6. Other options considered

- 6.1. Not applicable.

7. Summary

- 7.1 The annualised performance of the combined Haringey fund has declined in absolute terms by 9.96% per cent up to 30 June 2009, underperformed the gross benchmark by 2.43% and also underperformed the gross target by 4.07%.
- 7.2 Overall performance this quarter is below both benchmark and target.
- 7.3 There has been a measure of volatility in the market over the past period but overall, markets have risen.
- 7.4 In overall terms the budget is on target.

8. Head of Legal Services Comments

- 8.1 The Head of Legal Services has been consulted on the content of this report. The consideration of this report falls within the duties on the Committee, acting for the Administering Authority, in reviewing investment performance generally and the performance of specific investment fund managers. Such a review must always take into account the interests of stakeholders and beneficiaries.

9. Equalities & Community Cohesion Comments

- 9.1. There are no equalities issues arising from this report.

10. Consultation

10.1. Not applicable.

11. Service Financial Comments

11.1 Performance of our Fund Managers continues to be carefully monitored in the current market conditions. Capital continue to under perform both the benchmark and the target.

11.2 In overall terms the budget is on target. The current surplus is being monitored carefully so that any net gain is invested at the appropriate time in line with the agreed investment strategy. The majority of the current years in-house surpluses are earmarked to fund private equity investments.

12. Use of appendices /Tables and photographs

- 12.1. Appendix 1 Top ten shares held and fund holdings.
- 12.2. Appendix 2 Fund performance to 30 June 2009.
- 12.3. Appendix 3 Responsible Investments (Top ten holdings).
- 12.4. Appendix 4 Responsible Investments (Other holdings).
- 12.5. Appendix 5 Budget management to end of July 2009.

13 Local Government (Access to Information) Act 1985

Northern Trust performance monitoring reports.

Fund performance update report to Pensions Committee on 18 June 2009.

14 Investment performance reported at the March meeting of Pensions Committee

14.1 The investment performance of the Pensions fund was last reported to Pensions Committee in June 2009. That report covered the period up to 31 March 2009, at which time the following points were noted:

- Since monitoring against the new benchmark commenced on 1 April 2007, the combined Haringey fund has declined in absolute terms by 13.60% per cent up to 31 March 2009, underperformed the gross benchmark by 2.27% and also underperformed the gross target by 3.91%.

- There has been continuous uncertainty in the market over the past period due to a number of issues. These principally concerning the timings and pace of economic recovery. These have impacted upon the performance of our portfolio and are still ongoing. Up to the end of March 2009 performance by our Fund Managers was as follows:
 - Bernstein's Global Equity and UK Equity mandates have underperformed the gross targets by 12.56% and 9.35% respectively.
 - Fidelity's Bond mandate under performed the gross target by 1.70% and the Equity mandate under performed the gross target by 1.02% but achieved the benchmark.
 - Capital's Equity and Bond mandates are below target by 3.54% and 2.54%
 - ING are below target by 0.91%.

15. Investment performance for the combined Fund updated for this quarter

- 15.1 The last performance update to Pensions Committee on 18 June 2009 reminded trustees that our new investment structure was largely implemented on 16 March 2007. Therefore, this report shows performance monitoring against the new benchmarks from 1 April 2007.
- 15.2 Performance of the combined Haringey fund compared to benchmark and target for the three months and annualised 27 months periods to end of June 2009 are shown below. The target is shown gross of Fund Managers fees and assumes that returns above benchmark are achieved evenly throughout the year.

	3 months to end of June 2009	27 months to end of June 2009 (annualised)
	%	%
Overall fund performance	5.80	(9.96)
Benchmark	6.65	(7.53)
Performance versus benchmark	(0.85)	(2.43)
Overall fund performance	(5.80)	(9.96)
Target	(7.06)	(5.89)
Performance versus target	(1.26)	(4.07)

15.3 This shows that in the 27 months period to June 2009:

- The annualised performance of the combined Haringey fund has decreased in absolute terms by 9.96%, the fund under performed the new benchmark by 2.43% and under performed the target by 4.07%;
- The annualised position has marginally deteriorated since that report to the last meeting with the under performance versus target increasing from (3.91) to (4.07).

15.4 Appendix 1 shows the following for the combined fund as at end of June 2009 and 2008 for comparative purposes: (1) top ten shares held and (2) fund holdings.

16. Fund Manager Performance

16.1 Appendix 2 shows for each Fund Manager investment performance to end of June 2009, compared to benchmarks and targets as supplied by our custodian, Northern Trust. This is the ninth quarter since the new benchmarks were introduced, consequently, we have limited historic data.

16.2 The performance targets for each Fund Manager's mandates are shown below. They denote the percentage annualised return above benchmark over a rolling 3 year period. The table also includes Investec and Record for completeness. The contract with Alliance Bernstein was terminated on 16 June 2009 and the resulting assets transferred to Legal and General and invested in tracker funds as previously agreed. Consequently, detailed performance data in respect of these two companies is not included in the information below.

16.3 We have had 21 calls on the Pantheon Asia and USA funds totalling £9.8 million to date and although performance numbers are included there are not considered meaningful as a significant proportion of the portfolio is yet to be invested.

16.4 Targets are set out in the table below and are gross of fees.

	% Target above benchmark	% actual annualised performance above/(below) benchmark in the 27 months to June 2009	% actual annualised performance above/(below) target in the 27 months to June 2009
Capital - equities	2.0	(1.66)	(3.66)
Capital - bonds	1.0	(1.35)	(2.35)
Fidelity - equities	1.7	0.67	(1.03)
Fidelity - bonds	0.6	0.11	(0.49)
ING	1.0	(0.72)	(1.72)
Pantheon – private equity	0.75	N/A	N/A
Investec – active currency	2	N/A	N/A
Record – active currency	2	N/A	N/A

16.5 The latest quarterly meetings took place on 29 July 2009 between each Fund Manager (excluding Pantheon – where meetings are held half yearly) and the Head of Finance – Budgeting, Projects & Treasury. A summary of the key issues discussed at those meetings is set out below.

16.5.1 Legal and General

- Performance to date.
- Future outlook for markets.
- Review of our Responsible Investment policy.

16.5.2 Capital International

- Performance to date.
- Future outlook for markets.
- Review of our Responsible Investment policy.

16.5.3 Fidelity

- Performance to date.
- Future outlook for markets.
- Responsible Investments.

16.5.4 ING

- Performance to date.
- Volatility in the property market and future estimated returns.
- Investment opportunities to become fully invested to increased property benchmark.

16.5.5 Up to the end of June 2009 performance by our Fund Managers in annualised terms was as follows:

- Capital's Equity and Bond mandates are below target by 3.66% and 2.35%.
- Fidelity's Equity and Bond mandates under performed the gross targets by 1.03% and 0.49% respectively, although both mandates have marginally exceeded their benchmarks.
- ING are below target by 1.72%.

17. Conclusions

17.1 Since monitoring against the new benchmark commenced on 1 April 2007, the annualised performance of the combined Haringey fund has declined in absolute terms by 9.96% per cent up to 30 June 2009, under performed the gross benchmark by 2.43% and also under performed the gross target by 4.07%.

17.2 Regarding our Fund Managers, Capital are under performing the most.

17.3 Although equity and bond returns have been positive in the last quarter there are a number of ongoing issues which are likely to impact on future performance, and we are monitoring the position carefully. These include:

- The paying down of household, corporate and sovereign debt;
- The price of oil and commodities
- The trends of inflation/deflation
- Interest rates; and,
- Property prices and rental values.

18. Responsible Investments

18.1 At Pensions Committee on 23 June 2008 a review of the Fund's Responsible Investment Policy was considered and agreed by Trustees. One of the recommendations was that officer's monitor the Fund Managers approach to the revised Responsible Investment Policy.

18.2 Appendix 3 and 4 compares responsible investments information provided by the Council's two core Fund Managers for the quarter ending 30 June 2009 with the information supplied by LAPFF over the same time period for the Fund's top ten holdings of shares (Appendix 3) and engagement with other companies (Appendix 4) Where LAPFF have raised issues in companies where Haringey do not own shares, then this information has been excluded. This comparison will be made each quarter going forward as part of this report.

19. Budget Management

19.1 The budget monitoring analysis to period 4 (end of July 2009) is attached in Appendix 5.

19.2 Significant variances to date are:

- transfer values paid £316k and received (£1.705m) where the volume will vary by year and timing within the year ;
- the amount of lump sums (£387k) paid vary by year and timing within the year;
- investment income £3.087m is dependent upon companies invested in by our Fund Managers;
- employer contributions £187k are dependent on the number and grades of staff transferring into and out of the scheme;
- investment management expenses (£488k) are influenced by the timing of receipt of invoices from Fund Managers and market values.

19.3 In overall terms the budget is on target. The current surplus is being monitored carefully so that any net gain is invested at the appropriate time in line with the agreed investment strategy. The majority of current year's in-house surpluses are earmarked to fund private equity investments.

20. Invested cash

20.1 Following the strategic review of the Fund in March 2007 trustees approved an increase in property holdings from 6%-10%. An amount of cash equivalent to that increased holding of £18m was invested in the money market pending the identification of suitable investment opportunities by the property manager ING. To date, £8.65m has been drawn down by ING to fund investments in both UK and European property funds. The balance of £9.35m remains invested in fixed term deposits of up to one year pending further cash calls from ING.

20.2 The downturn in the property market has impacted on the timing of future cash calls such that the mandate is unlikely to be fully funded until 2010.

- 20.3 The strategic review of March 2007 also recommended that cash generated annually from surplus contributions, equivalent to £10m p.a be earmarked to fund a new private equity mandate managed by Pantheon. In the year to March 2009 £6.35m was transferred directly to Pantheon to fund cash calls on the mandate. The uncalled balance of £3.35 was added to the brought forward cash surplus that was set aside in 2007 to fund the mandate. As at 30 June 2009 £13.15m is invested by the Council on the Fund's behalf in fixed term deposits pending cash calls by Pantheon.
- 20.4 The Council's standard risk protocols are applied to all investments made on behalf of the pension fund.

APPENDIX 1

TOP TEN SHARES HELD

Shares	As at 30 June 2009			As at 30 June 2008		
	Rank	Percentage of Equities	Market Value	Rank	Percentage of Equities	Market Value
		%	£'000		%	£'000
Shell 'B' Ord	1	0.70	2,157	1	3.68	13,920
Roche	2	0.69	2,137			
HSBC	3	0.67	2,083	6	1.24	4,689
BP	4	0.65	2,019	2	2.91	11,023
Vodafone	5	0.61	1,909	3	2.15	8,149
SMC	6	0.42	1,314			
NTT Docomo	7	0.42	1,297			
Astra Zeneca	8	0.38	1,188	9	0.94	3,560
Aviva	9	0.36	1,110	7	1.00	3,810
Shell 'A'	10	0.35	1,085			
Glaxosmithkline				4	1.88	7,132
Royal Bank Scotland				5	1.74	6,591
BAE Systems				8	0.97	3,682
Barclays				10	0.92	3,476

FUND HOLDINGS

Fund Holdings	As at 30 June 2009		As at 30 June 2008	
	Percentage of Fund	Market Value	Percentage of Fund	Market Value
	%	£'000	%	£'000
UK equities	5.1	26,194	20.4	117,900
Overseas equities	12.9	65,840	22.0	126,846
Pooled investment vehicles	63.8	324,534	40.4	233,494
Index-linked securities	3.2	16,156	1.2	6,826
Fixed interest securities	3.5	17,608	3.4	19,786
Cash	5.5	27,819	4.6	26,466
Property	6.1	30,870	8.0	46,143
Totals	100.00	509,021	100.00	577,461

Appendix 3 – Pension Fund Top Equity Ten Holdings – Responsible Investment Activity - Quarter ending 30 June 2009

Top Ten Holdings & Percentage of Total Fund	Fidelity – Details of Responsible Investment Engagement	Capital International – Details of Responsible Investment Engagement	LAPFF Engagement
1. Shell 'B' Ord (0.70%)	No specific details received but see note below.	Capital have reported that they have not undertaken any engagement on an environmental, social or governance basis in quarter 2.	No activity this quarter.
2. Roche (0.69%)	"	"	"
3. HSBC (0.67%)	"	"	"
4. BP (0.65%)	"	"	"
5. Vodafone (0.61%)	"	"	"
6. SMC (0.42%)	"	"	"
7. NTT Docomo (0.42%)	"	"	"
8. Astra Zeneca (0.38%)	"	"	"
9. Aviva (0.36%)	"	"	"
10. Shell'A' (0.35%)	"	"	"

Note:

Fidelity explain that their engagement with companies is channelled primarily through their team of equity analysts. This contact includes quarterly face-to-face meetings with the CEO or FD, monthly contact with the Investor Relations team, periodic site visits to see the company's operations and attendance at analyst days hosted by the company. Dialogue encompasses all aspects of a company's business including strategy, operations, trading, governance, shareholder rights, environmental and social policies. Where there is a divergence of views or a matter of particular importance arises, FIL's corporate finance team may become involved. Matters involving corporate finance might include board and management composition, corporate strategy, specific corporate transactions and legal matters. FIL's proxy voting function also forms part of the corporate finance team and has a particular focus on remuneration-related issues.

Appendix 4

Comparison of Responsible Investment Activity Quarter ending 30 June 2009 – Core Fund Managers and Local Authorities Pension Fund Forum (LAPFF)

Fidelity	Capital International	LAPFF
<p>The Carbon Market During this quarter, Fidelity held discussions with RWE, one of the most carbon-intensive power generators in Europe around finding ways the Company could lower its carbon intensity.</p> <p>Renewable Power During Q2 Fidelity continued to monitor the progress power utility companies are making are making in the generation of energy from renewable sources. Fidelity met with Verbund, a large hydro generator in Austria who have acquired a number of hydro power plants from E.ON. Fidelity see this as a positive move towards the expansion of Verbund's clean and efficient generation strategy in Europe.</p>	<p>Tesco Tesco found itself the recipient of a shareholder resolution at its AGM. A consortium of shareholders, led by Unite, proposed several initiatives related to corporate responsibility. They requested that Tesco develop key performance indicators to measure compliance with stated policies; that the company should better manage labour issues in its UK meat and poultry supply chain in order to eliminate discrimination; and finally that it should add one of its non-executive directors to its Corporate Responsibility Committee. Capital held a call with Tesco to discuss this. Their representative responded as follows: supplier issues was an industry issue and the conflict between agency and full-time staff are not only applicable to Tesco. These cases also related to other companies in the supply chain. They did not think that the appropriate way to deal with these issues was via</p>	<p>M & S In Q1, LAPFF filed a shareholder resolution. The resolution called for the M&S to do everything possible to appoint an independent chairman by July 2010. The role of Chairman and Chief Executive is currently filled by one person Sir Stuart Rose. The resolution was voted on at the company's AGM in July. 37.7% of shareholders voted in favour of the LAPFF resolution, with abstentions taking the total not supporting management to over 40%. LAPFF is now looking forward to an immediate dialogue with the company about how it plans to respond. LAPFF also intend canvassing the views of other supporters of the resolution to elicit their views on the way forward.</p>

<p>Fidelity</p>	<p>Capital International</p>	<p>LAPFF</p>
<p><u>Sustainable Transport</u> During Q2 Fidelity discussed the technological solutions to reducing CO2 emissions with automakers BMW and Renault, including the use of hybrid vehicles, hydrogen fuel cells and the development of electric cars. Fidelity also met with automobile parts manufacturers Elriglinger to examine strategies for reducing emissions including its development of diesel particulate filters and Andritz which is working on bio fuel projects.</p>	<p>an AGM resolution. The representatives argued that the proponents had provided no evidence of abuses. Tesco confirmed it had visited all of its suppliers to review conditions. We asked whether the non-executive director suggestion was being considered. Tesco agreed that this had been the most sensible suggestion from the proponents. Tesco felt all of its board should be jointly responsible for corporate responsibility, and if it appointed one director to be head of corporate responsibility it would result in excessive external pressure on that individual. Tesco said it preferred to keep the status quo. As the shareholder suggestions were presented as a single resolution for shareholders to vote on, it was not possible to support some aspects of the plan while opposing others. As we did not agree that all of the suggestions had merit we voted with management against the proposal.</p>	<p><u>Governance reform</u> LAPFF will continue to push for governance reform following the current financial crisis and is continuing to undertake engagement with a number of financial institutions over issues such as remuneration and audit.</p>
<p><u>Child & Illegal Labour</u> In Q2 Fidelity discussed supply chain issues with Associated British Foods(ABF) owners of Primark . This follows ABF identifying cases amongst its suppliers of the employment of child labour and migrant labour being employed at wage rates below minimum</p>	<p><u>Corporate Governance</u> Telekom Austria Capital learnt in April that Telekom Austria was planning to extend its authority to issue convertible shares.</p>	

<p>Fidelity</p>	<p>Capital International</p>	<p>LAPFF</p>
<p>levels. Weapons Manufacturers During Q2 Fidelity discussed with BAE Systems, Rolls Royce and Safran their economic and reputational exposure to products which may result in institutional divestment.</p>	<p>The company had an existing five-year authority, which was due to expire, to issue equity or convertibles. The authority allowed for the issuance of equity with a potential dilution of 20%, which would have been detrimental to shareholders. Capital did not feel the authority was necessary, and generally prefer such requests to be made to shareholders annually as opposed to multi-year terms. Following discussions with Capital's sector analyst and other investors, the company finally decided against extending the authority, and took the strong action of removing the entire resolution from the agenda.</p> <p>Capital held discussions with several French companies over items on their shareholder meeting agendas. Capital frequently vote against numerous proposals on French ballots due to high dilution of shares, excessive stock option plans, large contract severance packages and incentive schemes that have little or no disclosure of performance targets. Severance payments in particular have attracted a lot of attention this year, and shareholders have the</p>	

<p>Fidelity</p>	<p>Capital International</p> <p>opportunity to vote on agreements in place for individual executives. It is common in France for these “golden parachute” payments to be worth two years’ annual cash compensation (salary and bonus). CGII commonly votes against these packages.</p> <p>Capital held discussions with L’Oreal and Veolia Environment prior to voting at their AGMs, to seek clarification and to provide feedback on resolutions that Capital would be unlikely to support.</p> <p>Capital also spoke with the French machinery firm Vallourec ahead of its AGM in May. We discussed the resolution to approve a severance payment to its company CEO, Philippe Crouzet. Vallourec was keen to secure shareholder support for the proposal as Riskmetrics—a key proxy service provider —recommended investors vote against it. We expressed our own concerns over the size of the severance package with the company. Their representatives were able to give Capital some assurances that the probable size of the payment would be much smaller than reported, and there were</p>	<p>LAPFF</p>
------------------------	---	---------------------

Fidelity	Capital International	LAPFF
	<p>limitations on the inclusion of bonus and share awards. As a result of the conversation it was felt that the company had considered the points raised and Capital were able to support the proposal. Though the resolution was adopted, a significant 37% of votes were cast against it.</p> <p>Company meetings:</p> <p>In addition to the meetings recorded above, Capital engaged with a number of companies, including Standard Chartered, to review a range of governance issues. Companies that consulted Capital on proposed changes to their executive remuneration policies include Inchape, Cable & Wireless and Home Retail Group.</p>	

APPENDIX 5

PENSIONS FUND

BUDGET MANAGEMENT - PERIOD 4 (END OF JULY 2009)

	2009/10 Budget £'000	Plan to period 4 £'000	Actual to period 4 £'000	Over/under (-) to Period 4 £'000	Explanations of variations
Income					
Contributions and benefits:					
Employee Contributions	(10,500)	(3,500)	(3,558)	(58)	
Employer Contributions	(34,700)	(11,566)	(11,379)	187	Dependent on number and grade of staff transferring into and out of scheme
Transfer Values Received	(4,000)	(1,333)	(3,038)	(1,705)	Volume and timing varies
Total income	(49,200)	(16,399)	(17,975)	(1,576)	
Expenditure:					
Pensions and other benefits	26,800	8,933	7,886	(1,047)	
Lump sums	3,500	1,166	779	(387)	Dependent upon the number of staff retiring and sums due.
Transfer values paid	4,000	1,333	1,649	316	Volume and timing varies
Refunds on contributions	50	17	1	(16)	
Administrative expenses	750	250	55	(195)	
Total expenditure	35,100	11,699	10,370	(1,329)	
Net addition from dealings with members	(14,100)	(4,700)	(7,605)	(2,905)	
Returns on Investment:					
Investment income	(18,300)	(6,100)	(3,013)	3,087	Dependent upon companies invested in by our Fund Managers.
Taxation	200	67		(67)	
Investment management expenses	3,600	1,200	712	(488)	Timing of receipt of Fund Managers invoices
Net return on investments	(14,500)	(4,833)	(2,301)	2,532	
Totals	(28,600)	(9,533)	(9,906)	(373)	