

PART 1 - PUBLIC

Decision Maker: Pension Investment Sub-Committee

Date: 10th February 2011

Decision Type: Non-Urgent Non-Executive Non-Key

Title: PENSION FUND PERFORMANCE

Contact Officer: Martin Reeves, Group Accountant (Technical)
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Chief Officer: Director of Resources

Ward: All

1. Reason for report

This report includes details of the investment performance of Bromley's Pension Fund for the first three quarters of the financial year 2010/11. It also contains information on general financial and membership trends of the Pension Fund and summarised information about early retirements.

RECOMMENDATION(S)

The Sub-Committee is asked to:

2.1 Note the report.

Corporate Policy

1. Policy Status: Existing policy. The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2007, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.
 2. BBB Priority: Excellent Council.
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Financial

1. Cost of proposal: No cost
 2. Ongoing costs: Recurring cost. Total administration costs estimated at £2.5m (includes fund manager/actuary fees, Liberata charge and officer time)
 3. Budget head/performance centre: Pension Fund
 4. Total current budget for this head: £31.6m expenditure (pensions, lump sums, etc); £40.3m income (contributions, investment income, etc); £482.3m total fund value at 31st December 2010)
 5. Source of funding: Contributions to Pension Fund
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Staff

1. Number of staff (current and additional): 0.6 FTE
 2. If from existing staff resources, number of staff hours: c 21 hours per week
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Legal

1. Legal Requirement: Statutory requirement. Local Government Pension Scheme (LGPS) Regulations 2007
 2. Call-in: Call-in is not applicable.
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Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 5,250 current employees; 4,487 pensioners; 3,864 deferred pensioners
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Ward Councillor Views

1. Have Ward Councillors been asked for comments? No.
2. Summary of Ward Councillors comments: N/A

3. COMMENTARY

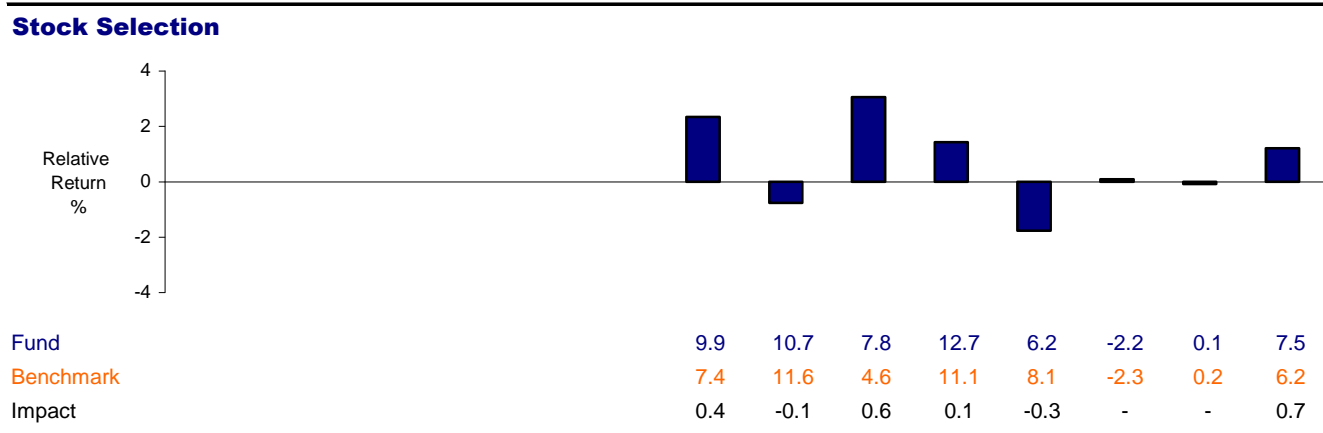
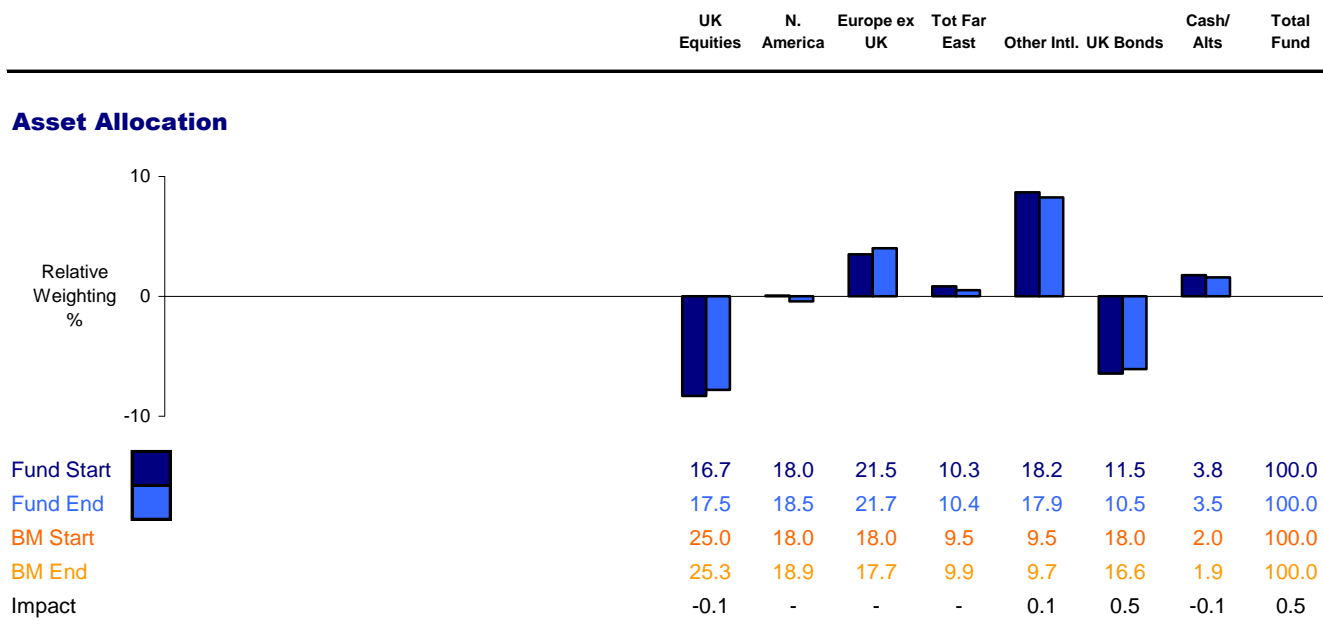
- 3.1 As the table and graph in paragraph 5.2 show, the total market value of Bromley's Fund has fluctuated considerably in the last few years. In 2002/03, the value fell by some 20% to £180m, but since then, in spite of some periods of volatility (most recently in the first and third quarters of 2008), a steady improvement was seen and the total value had increased to £357m as at 31st March 2008. In 2008/09, however, turmoil in financial markets caused the fund value to fall to £298.1m as at 31st March 2009, a fall of 16.5% in that year. During 2009/10, it increased steadily and ended the year at £446.4m as at 31st March 2010, a gain of almost 50% in the year. In 2010/11, the fund value has continued to fluctuate and had risen to £482.3m as at 31st December 2010. At the time of writing this report, the fund value stood at £476.4m (valuation as at 24th January 2011).
- 3.2 The report to the May meeting included details of the quarterly and cumulative performance of our two fund managers in 2009/10. These showed that Baillie Gifford were 6.3% above their benchmark for the year, while Fidelity were 4.4% above benchmark. An overall ranking of 2% was achieved in the year (1% being the highest in the WM Company local authority universe), which was a very good result after a reasonable year in 2008/09 and another good year in 2007/08. For comparison, the rankings in recent years were 33% in 2008/09, 5% in 2007/08, 100% in 2006/07 (equal worst in the whole local authority universe), 5% in 2005/06, 75% in 2004/05, 52% in 2003/04, 43% in 2002/03 and 12% in 2001/02. Given the long-term nature of pension fund liabilities, medium and long-term returns are of greater importance and these have been extremely good, with Bromley's Fund ranked in the 2nd percentile over the last 3 years, in the 1st percentile over 5 years and in the 5th percentile over 10 years. In 2010/11 to date, Bromley's Fund has achieved rankings of 94% in the June quarter and 6% in the September quarter. The rankings for the December 2010 quarter are not yet available and will be reported to the next meeting.

Performance data for 2010/11

- 3.3 Before 1st April 2006, the Fund's performance was measured against the local authority average and both Baillie Gifford and Fidelity were set the target of outperforming against that average by 0.5% over rolling three-year periods. When the Fund was restructured in 2006, however, both managers were set performance targets relative to the strategic benchmarks agreed from 1st April 2006. Baillie Gifford are now required to outperform the benchmark by 1.0% - 1.5% over three-year periods, while Fidelity's target is 1.9% outperformance over three-year periods. Since then, the WM Company has measured their results against these benchmarks instead of against its local authority indices and averages. At total fund level, however, it continues to use the local authority indices and averages and other comparisons with local authority averages may be highlighted from time to time to demonstrate, for example, whether the benchmark itself is producing good results. A summary of the two fund managers' performance in the first three quarters of 2010/11 is shown in the following table and more detail is provided in Appendices 1, 2 and 3. Local authority averages for the December quarter are not known yet and will be reported to the next meeting. Representatives of Fidelity will be present at the meeting to present a report on their performance.

Quarter	Baillie Gifford		Fidelity		Total Fund		LA Ave
	Benchmark	Return	Benchmark	Return	Benchmark	Return	Return
	%	%	%	%	%	%	%
Jun-10	-8.4	-7.6	-8.4	-9.0	-8.3	-8.3	-6.7
Sep-10	9.5	10.1	9.4	9.5	9.4	9.9	8.2
Dec-10	6.2	7.5	6.1	6.3	6.1	6.9	n/a
Cumulative	6.5	9.3	6.3	5.9	6.5	7.7	n/a

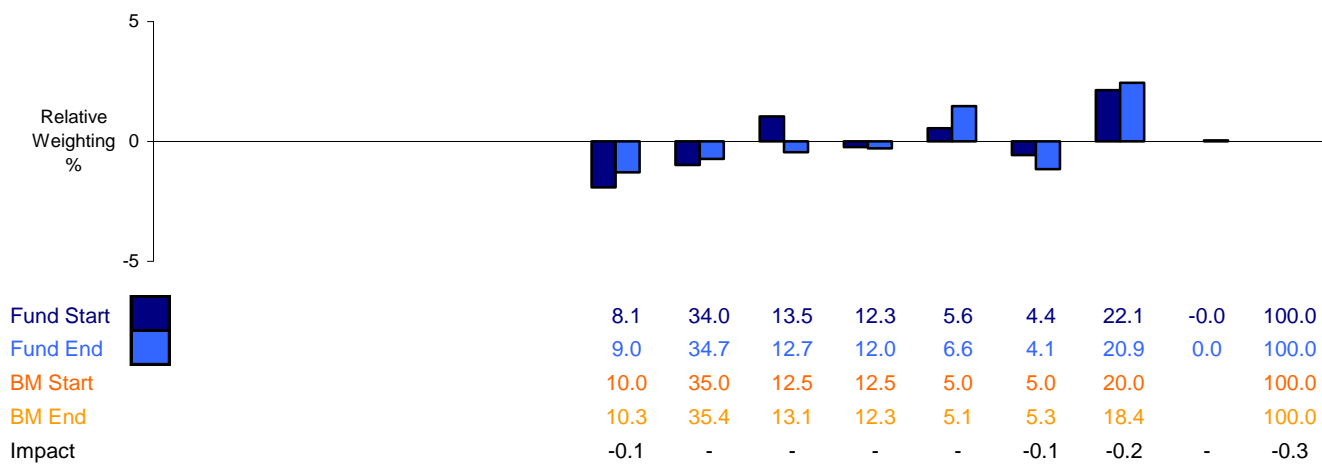
3.4 **Baillie Gifford** returned 7.5% in the December quarter (1.3% above benchmark) and achieved a cumulative return of 9.3% in the period 1st April 2010 to 31st December 2010 (2.8% above their benchmark). In the latest quarter, the WM Company attributed their relative outperformance to a combination of asset allocation (0.5%) and stock selection (0.7%). The main positive contributions from asset allocation and stock selection were from UK bonds and from European and UK equities respectively. These are represented in the following graphs.



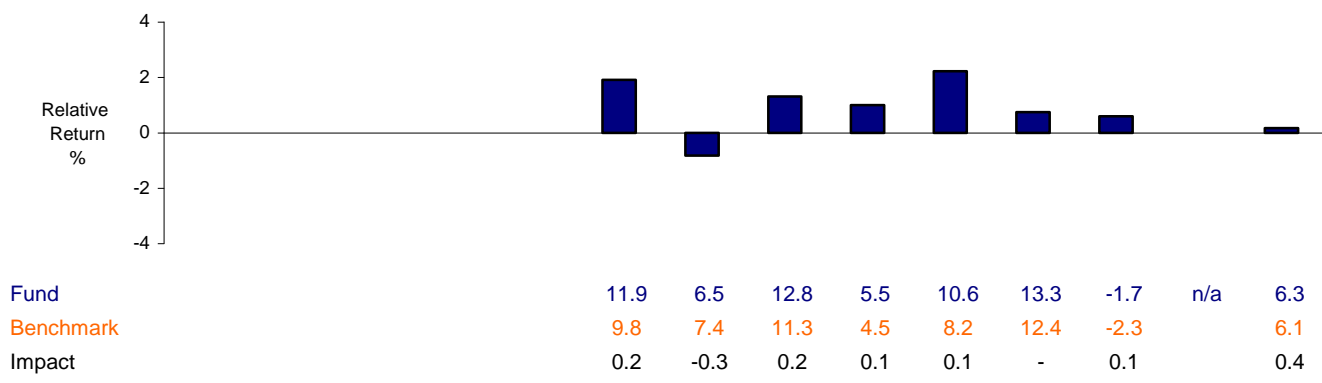
3.5 **Fidelity** returned 6.3% in the December quarter (0.2% above benchmark) and achieved a cumulative return of 5.9% in the first half year (0.4% below their benchmark). In the latest quarter, the WM Company attributed their relative outperformance to asset allocation (-0.3%) and stock selection (+0.4%). The negative asset allocation impact was mainly in UK Bonds, while the main stock selection impacts were seen in North American and Global equities. These are represented in the following graphs.

Global Equit UK Equities N. America Europe ex UK Pacific Japan UK Bonds Cash/ Alts Total Fund

Asset Allocation



Stock Selection



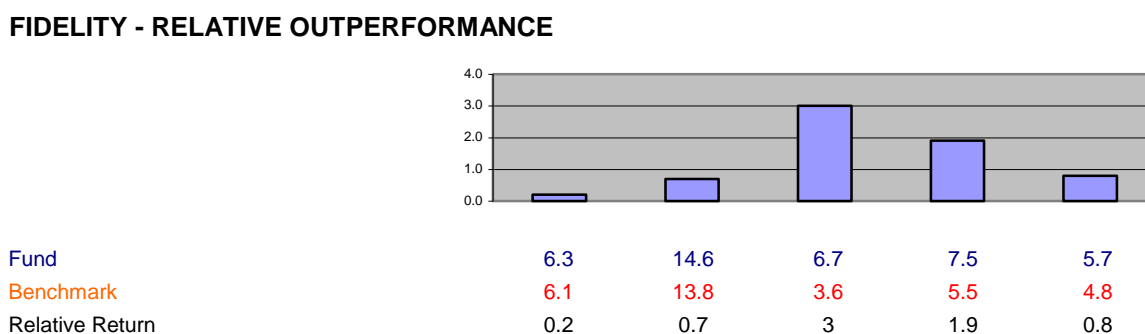
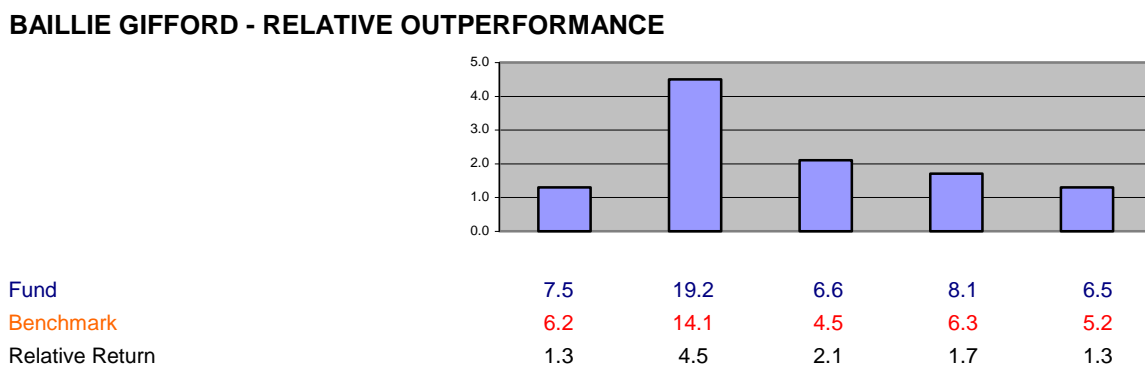
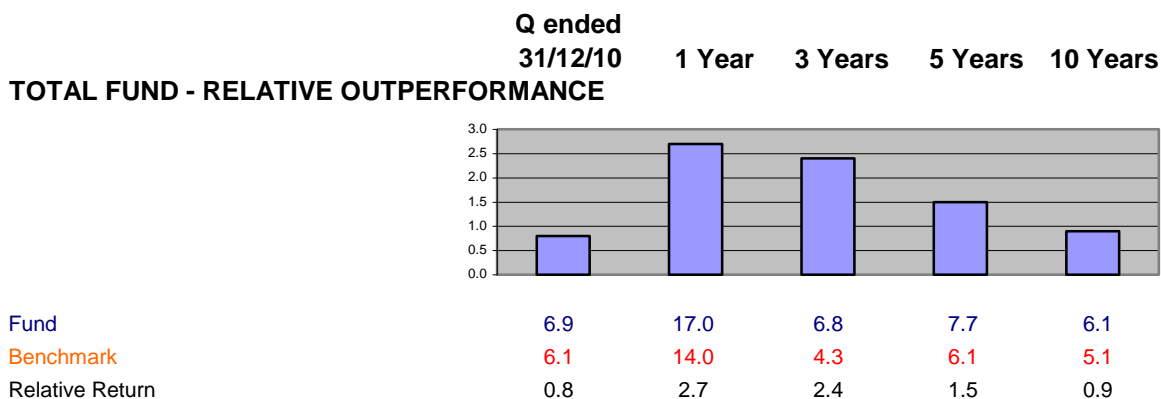
Medium and long-term performance data

3.6 The table below sets out comparative returns over 1, 3, 5 and 10 years for both Baillie Gifford and Fidelity for periods ended 31st December 2010 and 31st March 2010. Baillie Gifford's 1, 5 and 10-year returns to December 2010 (19.2%, 8.1% and 6.5% respectively) are better than those of Fidelity (14.6%, 7.5% and 5.7% respectively), although Fidelity's 3-year return (6.7%) is marginally better than that of Baillie Gifford (6.6%). Performance since the revised benchmarks were adopted in 2006 has been particularly strong.

	Baillie Gifford			Fidelity			
	Return	BM	+/-	Return	BM	+/-	LA Ave
	%	%	%	%	%	%	%
Periods to 31/12/10							
1 year (1/1/10-31/12/10) - annualised	19.2	14.1	4.5	14.6	13.8	0.7	n/a
3 years (1/1/08-31/12/10) - annualised	6.6	4.5	2.1	6.7	3.6	3.0	n/a
5 years (1/1/06-31/12/10) - annualised	8.1	6.3	1.7	7.5	5.5	1.9	n/a
10 years (1/1/01-31/12/10) - annualised	6.5	5.2	1.3	5.7	4.8	0.8	n/a
Periods to 31/3/10							

1 year (1/4/09-31/3/10) - annualised	51.3	42.3	6.3	45.9	39.8	4.4	35.2
3 years (1/4/07-31/3/10) - annualised	7.2	4.6	2.5	7.6	3.0	4.4	1.7
5 years (1/4/05-31/3/10) - annualised	10.2	8.5	1.6	10.1	7.6	2.3	7.1
10 years (1/4/00-31/3/10) - annualised	6.9	5.8	1.1	5.0	4.1	0.8	3.8

3.7 The following graphs look in more detail at performance relative to benchmark in the medium and long term for the whole fund and for Baillie Gifford and Fidelity individually.



LGPS Investment Regulations – Requirement for separate bank account

3.8 In December 2009, the Department for Communities and Local Government issued new investment regulations that came into force on 1st January, although some of the changes therein do not need to be implemented until 1st April 2011. These primarily comprise putting in place a separate bank account for the Pension Fund and making arrangements to ensure that surplus pension fund revenue cash is invested separately. Day to day transactions of the Pension Fund are accounted for separately within the Council's financial system and the Council has opened a new bank account with HSBC for its Pension Fund, to become active on 1st April 2011. It is not intended to change all the Council's systems (payroll, payments, income, etc) to accommodate this new account, but instead transfers will be made monthly or weekly between the Council's own bank account and the Pension Fund account to reflect Pension Fund cash

balances. With regard to the separate investment of Pension Fund cash, an agreement is in the process of being drawn up between the two parties that would enable the authority to continue to pool its cash balances and to allocate a proportion of the interest earned to the Fund, as it has always done.

Early Retirements

3.9 A summary of early retirements by employees in Bromley's Pension Fund in the current year and in previous years is shown in the table below. With regard to retirements on ill-health grounds, this allows a comparison to be made between their actual cost and the cost assumed by the actuary in the triennial valuation. If the actual cost significantly exceeds the assumed cost, the actuary will be required to consider whether the employer's contribution rate should be reviewed in advance of the next full valuation. The actuary does not make any allowance for other early retirements, however, because it is the Council's policy to fund these in full by additional voluntary contributions. The average cost of ill-health retirements over the three years 2004 to 2007 was close to the actuary's annual estimate of £375,000 per annum (in the 2004 actuarial valuation) and this will have had very little impact on the actuarial valuation as at 31st March 2007. The cost of other retirements in the same 3-year period averaged around £284,000 per annum. In the latest actuarial valuation (as at 31st March 2007), the actuary assumed a figure of £800,000 per annum for ill-health retirements for the three years from 2008/09. The total of ill-health retirements in 2008/09 was well below the estimate, while other retirements were slightly below average. In 2009/10, there were only 5 ill-health retirements with a total long-term cost of only £45,000, but the total of other retirements (£1,033,000) was considerably higher than in recent years. In the first three quarters of 2010/11, there was only one ill-health retirement (£94,000) and other retirements totalled £210,000.

Long-term cost of early retirements	Ill-Health		Other	
	No	£000	No	£000
Qtr 3 – Dec 10 - LBB	-	-	1	19
- Other	1	94	1	4
- Total	1	94	2	23
2010/11 to date – LBB	-	-	9	149
- Other	1	94	5	61
- Total	1	94	14	210
Actuary's assumption – 2008 to 2010		800		N/a
- 2004 to 2007		375		N/a
Previous years - 2009/10	5	45	21	1,033
- 2008/09	6	385	4	256
- 2007/08	11	465	11	260
- 2006/07	8	296	9	277
- 2005/06	12	371	5	342
- 2004/05	16	533	13	232

4. POLICY IMPLICATIONS

4.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations 2007, for the purpose of providing pension benefits for its employees. These regulations allow local authorities to use all the

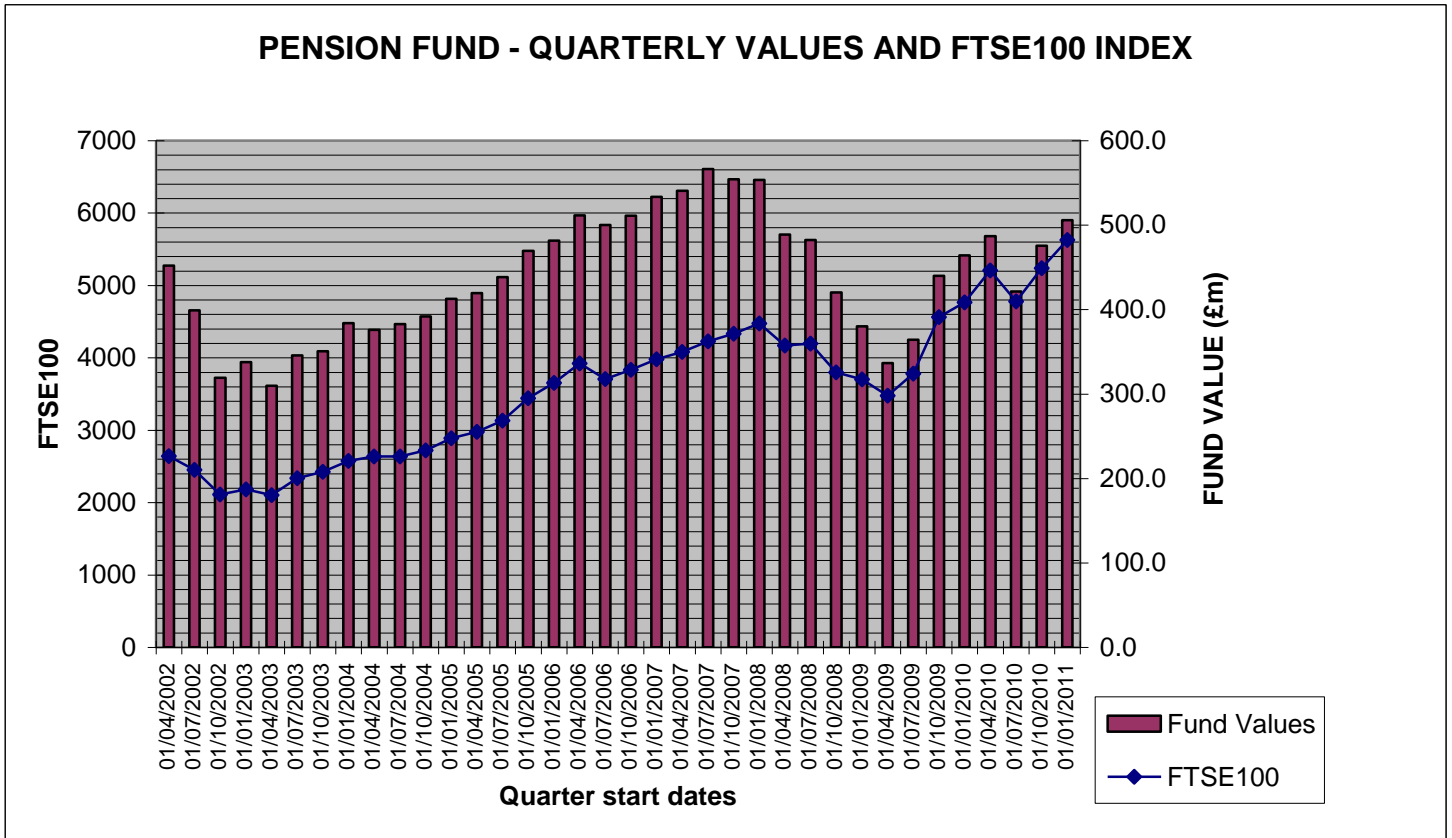
established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

- 5.1 Details of the actual position to 31st December 2010 for the 2010/11 Pension Fund Revenue Account are provided in Appendix 4 together with fund membership numbers. A net surplus of £7.0m was achieved in the first three quarters and total membership numbers rose by 210.
- 5.2 Changes in the Fund's Market Value are shown in the following table, together with details of distributions of the revenue fund surplus cash to the fund managers and changes in the value of the FTSE 100 index. The graph below plots movements in the fund value and in the FTSE index. Members will note that, in recent years, the total fund value has fluctuated significantly, having reduced by 16.6% (£59m) in 2008/09 before rising to £446.4m in 2009/10 (an increase of 50% in the year). In 2010/11, it lost ground initially but had increased to £482.3m as at 31st December 2010. The valuation at the time of writing this report (24th January) had fallen slightly to £476.4m. Also of note, although not entirely surprising, is the fact that the fund value tracks the movement in the FTSE 100 fairly closely, even though, since 2006, only around 30% of the fund has been invested in the UK equity sector.

Market Value as at	Fidelity	Baillie Gifford	CAAM	Total	Revenue Surplus Distributed to Managers	FTSE 100 Index
	£m	£m	£m	£m	£m	
31 st March 2002	112.9	113.3	-	226.2	0.5	5272
31 st March 2003	90.1	90.2	-	180.3	-	3613
31 st March 2004	112.9	113.1	-	226.0	3.0	4386
31 st March 2005	126.6	128.5	-	255.1	5.0	4894
31 st March 2006	164.1	172.2	-	336.3	9.1	5965
31 st March 2007	150.1	156.0	43.5	349.6	4.5	6308
31 st March 2008	151.3	162.0	44.0	357.3	2.0	5702
31 st March 2009	143.5	154.6	-	298.1	4.0	3926
31 st March 2010	210.9	235.5	-	446.4	3.0	5680
30 th June 2010	191.9	217.6	-	409.5	-	4917
30 th September 2010	209.2	239.6	-	448.8	-	5549
31 st December 2010	224.1	258.2	-	482.3	1.0	5900

PENSION FUND - QUARTERLY VALUES AND FTSE100 INDEX



Non-Applicable Sections:	Legal and Personnel Implications
Background Documents: (Access via Contact Officer)	Analysis of portfolio returns (provided by WM Company). Monthly and quarterly portfolio reports of Fidelity and Baillie Gifford.

Returns for quarter ended 31 December 2010

Baillie Gifford	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	25	7.4	17.5	9.9
Overseas equities				
North America	18	11.6	18.5	10.7
Europe	18	4.6	21.7	7.8
Far East	9.5	11.1	10.4	12.7
Other Int'l	9.5	8.1	17.9	6.2
UK bonds	18	-2.3	10.5	-2.2
Cash/other	2	0.2	3.5	0.1
Total assets	100	6.2	100.0	7.5

Fidelity	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	35.0	7.4	34.7	6.5
Overseas equities				
USA	12.5	11.3	12.7	12.8
Europe	12.5	4.5	12.0	5.5
Japan	5.0	12.4	4.1	13.3
S E Asia	5.0	9.0	6.6	10.6
Global	10.0	9.8	9.0	11.9
UK bonds	20.0	-2.3	20.9	-1.7
Cash/other	-	0.1	0.0	n/a
Total assets	100.0	6.1	100.0	6.3

Fidelity's UK equity holding above (34.7% of portfolio) includes 1.0% non-UK equities, in accordance with the agreement by the Sub-Committee at its meeting on 3 May 2005 that their UK equity manager could invest up to 20% of his portfolio in non-UK equities.

From 1st April 2008, both fund managers have operated under the same benchmark for UK equities (FTSE All Share index). Previously, Baillie Gifford had been using FTSE 100.

Returns for quarter ended 30 September 2010

Baillie Gifford	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	25	13.6	16.7	14.1
Overseas equities				
North America	18	5.8	18.0	6.3
Europe	18	13.6	21.5	13.9
Far East	9.5	7.1	10.3	7.9
Other Int'l	9.5	12.1	18.2	13.3
UK bonds	18	4.2	11.5	5.1
Cash/other	2	0.2	3.8	0.4
Total assets	100	9.5	100.0	10.1

Fidelity	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	35.0	13.6	34.0	14.4
Overseas equities				
USA	12.5	5.7	13.5	5.1
Europe	12.5	13.2	12.3	10.5
Japan	5.0	-0.0	4.4	1.9
S E Asia	5.0	13.0	5.6	11.2
Global	10.0	8.1	8.1	11.6
UK bonds	20.0	4.3	22.1	4.7
Cash/other	-	0.1	0.0	n/a
Total assets	100.0	9.4	100.0	9.5

Fidelity's UK equity holding above (34.0% of portfolio) includes 0.9% non-UK equities, in accordance with the agreement by the Sub-Committee at its meeting on 3 May 2005 that their UK equity manager could invest up to 20% of his portfolio in non-UK equities.

From 1st April 2008, both fund managers have operated under the same benchmark for UK equities (FTSE All Share index). Previously, Baillie Gifford had been using FTSE 100.

Returns for quarter ended 30 June 2010

Baillie Gifford	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	25	-11.8	16.6	-6.6
Overseas equities				
North America	18	-10.3	19.1	-11.5
Europe	18	-14.4	19.7	-10.8
Far East	9.5	-9.6	10.5	-11.2
Other Int'l	9.5	-6.5	17.7	-6.5
UK bonds	18	3.2	13.9	2.3
Cash/other	2	0.2	2.5	-0.0
Total assets	100	-8.4	100.0	-7.6

Fidelity	Benchmark Weighting	Benchmark Returns	Portfolio Weighting	Portfolio Returns
	%	%	%	%
UK equities	35.0	-11.8	33.3	-11.8
Overseas equities				
USA	12.5	-10.3	12.9	-12.2
Europe	12.5	-14.1	11.5	-15.9
Japan	5.0	-7.9	5.1	-9.1
S E Asia	5.0	-7.7	6.1	-8.2
Global	10.0	-11.3	10.8	-9.5
UK bonds	20.0	3.3	20.3	3.1
Cash/other	-	0.1	0.0	n/a
Total assets	100.0	-8.4	100.0	-9.0

Fidelity's UK equity holding above (33.3% of portfolio) includes 0.9% non-UK equities, in accordance with the agreement by the Sub-Committee at its meeting on 3 May 2005 that their UK equity manager could invest up to 20% of his portfolio in non-UK equities.

From 1st April 2008, both fund managers have operated under the same benchmark for UK equities (FTSE All Share index). Previously, Baillie Gifford had been using FTSE 100.

PENSION FUND REVENUE ACCOUNT AND MEMBERSHIP

	Final Outturn 2009/10 £'000's	Estimate 2010/11 £'000's	Actual to 31/12/10 £'000's
INCOME			
Employee Contributions	6,153	6,300	4,460
Employer Contributions	23,028	23,000	16,310
Transfer Values Receivable	4,457	4,000	3,200
Investment Income	7,141	7,000	6,240
Total Income	<u>40,779</u>	<u>40,300</u>	<u>30,210</u>
EXPENDITURE			
Pensions	18,350	19,000	14,400
Lump Sums	5,858	6,000	5,150
Transfer Values Paid	4,223	4,000	2,510
Administration	2,948	2,500	1,090
Refund of Contributions	12	100	10
Total Expenditure	<u>31,391</u>	<u>31,600</u>	<u>23,160</u>
Surplus/Deficit (-)	<u>9,388</u>	<u>8,700</u>	<u>7,050</u>
MEMBERSHIP			
	31/03/2010		31/12/2010
Employees	5,360		5,251
Pensioners	4,413		4,507
Deferred Pensioners	3,607		3,832
	<u>13,380</u>		<u>13,590</u>