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BRENT COUNCIL

FORWARD TOGETHER

Brent Pension Fund Sub-Committee

Tuesday, 30 November 2010 at 6.30 pm
Committee Room 4, Brent Town Hall, Forty Lane, Wembley, HA9 9HD

Membership:

Members	first alternates	second alternates
Councillors:	Councillors:	Councillors:
S Choudhary (Chair)	Denselow	Gladbaum
Mrs Bacchus	A Choudry	Daly
Crane	Harrison	Hector
Mitchell Murray	Hirani	Hossain
Brown	CJ Patel	
Hashmi	CJ Patel	
BM Patel	HB Patel	Baker

Non Voting Co-opted Members

George Fraser	GMBU
Ashok Patel	College of North West London

For further information contact: Joe Kwateng, Democratic Services Officer: (020) 8937 1354, joe.kwateng@brent.gov.uk

For electronic copies of minutes, reports and agendas, and to be alerted when the minutes of this meeting have been published visit:
www.brent.gov.uk/committees

The press and public are welcome to attend this meeting

(The meeting will be preceded by a training session at 5.30pm on private equity by Capital Dynamics).

Agenda

Introductions, if appropriate.

Apologies for absence and clarification of alternate members circulated to members of the Sub-Committee only.

Ward affected: All Wards; ***Contact Officer**:* Martin Spriggs, Exchequer and Investment

Tel: 020 8937 1472
martin.spriggs@brent.gov.uk

8 Hedge Fund Investment - proposal by Fauchier Partners 29 - 32

This report from the Head of Exchequer and Investment sets out proposals by Fauchier Partners, hedge fund investment managers that Brent should join the Jubilee Special Situations Fund.

Ward affected: All Wards; ***Contact Officer**:* Martin Spriggs, Exchequer and Investment

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martin.spriggs@brent.gov.uk

9 Brent Pension Fund - socially responsible investment 33 - 48

This report reviews Socially Responsible Investment (SRI) policies for the Brent Pension Fund.

Ward affected: All Wards; ***Contact Officer**:* Martin Spriggs, Exchequer and Investment

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10 Any other urgent business

Notice of items to be raised under this heading must be given in writing to the Democratic Services Manager or his representative before the meeting in accordance with Standing Order 64

11 Date of next meeting

Tuesday 1 March 2011 at 6.30pm

Please remember to ***SWITCH OFF*** your mobile phone during the meeting.

- The meeting room is accessible by lift and seats will be provided for members of the public.

- Toilets are available on the second floor.
- Vending machines are available on the first floor near the Paul Daisley Hall.
- A public telephone is located in the foyer on the ground floor, opposite the Porters’ Lodge

LONDON BOROUGH OF BRENT

MINUTES OF THE BRENT PENSION FUND SUB-COMMITTEE
Tuesday, 28 September 2010 at 6.30 pm

PRESENT: Councillor S Choudhary (Chair) and Councillors Mrs Bacchus, Crane, Mitchell Murray, Hashmi and BM Patel

1. **Declarations of Personal and Prejudicial Interests**

   None declared.

2. **Minutes of the Previous Meeting held on 29 June 2010**

   RESOLVED:-

   that the minutes of the previous meeting held on 29 June 2010 be approved as an accurate record of the meeting.

3. **Matters Arising**

   Monitoring Activity for the quarter ended 31 March 2010 - BP

   Valentine Furniss (Independent Adviser) enquired on the impact of the income stream in view of BP's problems in relation to oil spill in the Gulf of Mexico.

   In reply, Martin Spriggs (Head of Exchequer and Investment) advised that BP had suspended dividends because of reduced income, however share prices had since risen and the situation had stabilised, so the Council had decided to retain the shares.

   Urgent action on currency – amendment to Statement of Investment Principles

   Martin Spriggs advised that AllianceBernstein had re-established the currency hedge in August.

4. **Pension Fund Accounts 2009/10**

   Martin Spriggs introduced the report and advised that the main change from the draft account presented in June was to amend market values of a selection of funds to agree with the valuations recorded by the custodians as set out in appendix two of the Annual Governance report.

   Paul Viljoen (Audit Commission) introduced the Annual Governance report which requested Members to consider matters raised in the report in respect of financial statements, to note the adjustments to the financial statement as set out in the report, approve the letter of representation on behalf of the Council and agree to the Council's response to the proposed action plan. Paul Viljoen also advised that the Audit Commission proposed to increase the Pension Fund audit by £3,000 based on additional work required to resolve issues.

During Members' discussion, the Chair sought information with regard to the error identified in investment commitments. Councillor Crane enquired whether the Audit Commission fee was fixed or negotiable. Councillor Hashmi asked for further details as to the increase in the fee.

In reply, Paul Viljoen advised that in respect of investment commitments, Capital Dynamics had miscalculated in their original evaluation, however this had been identified by the Audit Commission and duly corrected by the Council. He confirmed that Audit Commission fees were set on a scale basis dependent on the size and type of organisation.

RESOLVED:-

that the report on the Pension Fund Accounts 2009/10 be noted.

5. **WM Annual Report**

Lynn Coventry (WM) presented the report and began by informing Members of the performance of equities, bonds, alternatives and currencies for the year 2009/10. She then described the longer term performance of assets and the level of inflation for 3, 5, 10 and 20 year periods. In respect of performance relative to market indices, Lynn Coventry advised that because of increased manager and administrative fees, investors would want to see increased returns and it was anticipated that UK exposure would continue to fall. Lynn Coventry then referred to local authority average asset allocation as of end of March 2010. Members noted that UK equities only accounted for 44% of total equities, whilst there had been significant movement to alternatives.

Members then noted updates to the Council's Fund in relation to a number of measures. Lynn Coventry concluded by advising that the overall Fund return was 29%, 0.8% behind the benchmark of 29.8%, whilst the WM local authority average return was 35.2%. The three year period Fund return of -3.9% was 3.3% per annum below the benchmark, whilst over the ten year period the Fund return of 1.9% was 0.3% below the benchmark of 2.2%, and below the WM average of 3.8%.

Martin Spriggs added that in relation to the 31% of the Fund being managed internally, this also included private equity management which was undertaken by different managers, so in reality the proportion of the Fund internally managed was considerably less. He advised that the infrastructure fund invested by Henderson had performed well and had started to recover losses from the previous two years. Although the Fund's return had fallen behind the benchmark primarily due to stock allocation, the 29% return still represented a strong one.

Valentine Furniss enquired whether AllianceBernstein's performance compared to its competitors was amongst the lowest performing. Lynn Coventry confirmed that this was the case.

6. **Monitoring Report on Fund Activity for the Quarter Ended 30 June 2010**

Martin Spriggs introduced the report and confirmed that equity markets had fallen sharply during this quarter. However, a recent revival in equity meant that the Fund's reported drop in value of £455m to £424.6m had been reversed (to £465m). He advised that the Fund had underperformed both in terms of the benchmark figure and in comparison with other local authorities. This was principally due to underperformance in both asset allocation and stock selection. Members noted that interest rates were likely to remain stable. The Committee were provided with details in respect of asset allocation and investment returns in individual markets. Martin Spriggs reported that the head of Gartmore, Gervais Williams had resigned, however he been replaced by a well qualified and experienced colleague, Adam McConkey. The Council had been reassured that the Gartmore Team remained strong. However, exposure is being reduced as there are wider concerns about the market reaction to the manager leaving and to problems at Gartmore itself.

Valentine Furniss circulated a paper detailing index returns for the period 1 July to 17 September 2010. Valentine Furniss reported that global GDP was forecast to increase by 4.6% for this year and by 4.3% next year. Other positive factors included the fact that exports were quite healthy and there was strong growth in Europe. Problems continued to remain in respect of high national deficits, high rates of unemployment and the collapse of residential property prices. Valentine Furniss felt that a double dip recession and a break-up of the Eurozone were unlikely. Valentine Furness commented that a 7-8% return of the Council's Pension Fund would be an achievement considering the circumstances this year.

During discussion, Councillor Hashmi commented that IMF had been quite bullish about the UK economy and he sought views with regard to the outcome of the Comprehensive Spending Review (CSR). Councillor Mitchell Murray expressed concerns in respect of the CSR and the prospect of a double dip recession. She also expressed some doubts over India's economic development. Councillor Crane commented that CSR would affect local authorities and the public sector generally more than the economy overall. The Chair sought views on measures by the USA to ban countries from exporting to them where these countries had deliberately kept their currency value low.

In reply to the issues raised, Valentine Furniss felt that the austerity measures expected in the CSR had been widely reported for some time and that public funded bodies anticipated that further significant savings would be required. He suggested that the positive outcomes would outweigh the negative ones, whilst he remained optimistic about India's economic growth, stating that the right infrastructure was being put in place and considerable investment continued. Valentine Furniss advised that the USA needed to be mindful in respect of banning exports from other countries, particularly as there were other economies that these countries could turn to. He added that there were various trading groups performing well, including Asia, South America and also the Eurozone to a lesser extent.

Clive Heaphy (Director of Finance and Corporate Resources) added that it would be a few weeks after the announcement of CSR was made before local authorities would be able to assess the impact upon their budgets. He advised that it was likely that sharper and deeper cuts would be made in the early years, whilst spending was likely to increase as the date of the next General Election neared.

RESOLVED:-

that the monitoring report on Fund Activity for the Quarter Ended 30 June 2010 be noted.

7. **Investment in Private Equity**

Martin Spriggs introduced the report and advised that private equity investments were long term investments, with private equity returning 5-10% above public equity markets over the long term. A revised private equity programme had been agreed in 2007 with a target exposure of 8% with a view to rise to 10% in the long term. However, falling markets in 2007/09 meant that the current investment programme may take private exposure to around 11% of the Fund in 2011/12. The programme had recently been reviewed and it had been identified that there were opportunities for good returns and to increase exposure to emerging markets. Martin Spriggs advised that it was being recommended to invest £10m in the Solar Fund in the USA as it would offer the potential to provide both short and long term returns.

During discussion, Councillor Hashmi expressed approval in the investing in the Solar Fund and Councillor Crane added that it would provide a good opportunity to generate returns. Councillor Mitchell Murray enquired whether investment in the Solar Fund would help the Council achieve its green targets. Councillor Bacchus felt it was prudent to consider investment in emerging markers.

Valentine Furniss enquired what percentage of the Fund the Solar Fund would represent. Martin Spriggs advised that it would represent 10% of funds in private equity and 1.5% of the total Fund overall. He advised that the investing in the Solar Fund was a business decision, but that it would also add to the Council's green credentials.

RESOLVED:-

(i) that the revised investment programme be agreed; and

(ii) that investment in the Solar Fund be agreed.

8. **Date of Next Meeting**

It was noted that the next meeting was scheduled to take place on Tuesday, 30 November 2010 at 6.30 pm.

9. **Any Other Urgent Business**

None.

10. **Exclusion of Press and Public**

This item was not for publication as it relates to the following category of exempt information as specified in the Local Government Act 1972 namely:
Information relating to the financial or business affairs of any particular person (including the authority holding that information).

Review of Investment Mandate

Members had before them a report in respect of the review of an investment mandate. It was recommended that the manager be replaced by the appointment of an alternative. Martin Spriggs suggested that Members meet with the proposed alternative organisation to consider their suitability to be appointed.

During discussion, it was agreed that a meeting with the proposed alternative organisation take place on 13 October 2010 at 1.30 pm and that information also be provided on alternative organisations at the meeting by way of comparison.

RESOLVED:-

(i) that the recommendations as set out in the report be agreed; and

(ii) that a meeting with the proposed alternative organisation take place on 13 October 2010 at 1.30 pm to assess their suitability and that information be provided on a second alternative organisation at the meeting by way of comparison.

The meeting closed at 8.30 pm

S CHOUDHARY
Chair

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	Pension Fund Sub Committee 30 November 2010 **Report from the Director of Finance and Corporate Services**
	Wards Affected: ALL

Monitoring report on fund activity for the quarter ended 30 September 2010

1. SUMMARY

This report provides a summary of fund activity during the quarter ended 30th September 2010. It examines the actions taken, the economic and market background, and investment performance, as well as commenting on events in the quarter. The main points arising are:

a) Equity markets rose sharply during the quarter, recovering the losses sustained in the previous quarter. Other markets also rose, but less rapidly.

b) The Fund has risen in value from £424.6m to £454.1m, and has outperformed its benchmark over the quarter (0.8%) as a result of stock selection (outperformance in bonds, GTAA and private equity). The Fund underperformed the average local authority fund (-1.4%), mainly as a result of asset allocation (higher exposure to alternatives / lower exposure to equities). Over one year, the Fund has outperformed its benchmark (0.1%) as a result of poor returns from asset allocation (-0.5 – higher exposure to alternatives and bonds / lower exposure to equities, property and GTAA) offset by good stock selection (+0.6% - UK equities, bonds, private equity and GTAA, offset by poor performance in overseas equities and hedge funds). Over one year, the Fund has also underperformed the average fund (-3.4%) as a result of lower exposure to equities / higher exposure to alternative assets and poor performance in global equities.

2. RECOMMENDATIONS

Members are asked to note this report.

3 DETAIL

ECONOMIC AND MARKET BACKGROUND - QUARTER ENDED 30TH SEPTEMBER 2010

3.1 Equity markets rose during the quarter on the bases of world economic growth and the likelihood of renewed Quantitative Easing in USA and elsewhere. The

UK rose by 13%, USA 11%, Germany 10%, and HongKong 11%. The Japanese market was stable. The UK economic background was:

- UK base rates remained at 0.5%. Medium and long-term interest rates fell during the quarter. Concerns about the European banking system and various eurozone countries (Greece, Portugal and Spain) have affected these markets, but UK has benefited from a safe haven status.The Quantitative Easing programme in UK has been suspended, but may restart.
- Headline inflation (RPI) rose by 4.5% in the year to October (4.7% August), and the Index of Consumer Prices (CPI) rose by 3.2% (3.1% August). It is expected that inflation may fall over a two year period as spare capacity and low pay increases bear down on prices, but it is expected that CPI will be above the Bank of England 2% target during 2011.
- Average earnings growth (including bonuses) was 2.2% p.a. in September (1.8% July), below the Bank of England's 'danger level' (4.5%). Unemployment has fallen to 1.46m, but may rise as public expenditure is reduced and taxes raised following the recent budget.
- The UK economy grew by 0.8% in Q3 2010 (2.8% over a year). GDP is expected to grow by 2% in 2010 (and 1% / 2% in 2011).
- It has been anticipated that consumer spending will fall, though retail sales were up 0.5% in the year to September. The squeeze on incomes, and the decline in equity withdrawal from the housing market following price falls, may depress demand. Although, house prices have risen by 1.4% over one year to October (Nationwide), recent figures have shown falling prices. Mortgage approvals are only 60% of their level two years ago. Capital Economics still expects further house price falls (15%/20%).

In summary,the recession has ended but interest rates are expected to remain low. The government was using both fiscal and monetary policy to combat the downturn, but fiscal policy will be tightened over the next five years. The recovery is expected to be slow with occasional setbacks, but sentiment has improved considerably.

3.2 Central banks have co-ordinated activity to supply liquidity to markets so that credit is available to support economic activity. It is expected that the USA economy may grow by 3% in 2010 (but only 2% in 2011) following tax cuts, interest rate cuts, and quantitative easing (QE) programmes. Improved payroll data, strong retail sales and a rebound in home construction had indicated that a recovery was underway. Recent figures have shown the recovery to be faltering, but the reintroduction of $600b in QE may support demand. It is anticipated that company earnings will also improve. It is expected that Eurozone GDP will grow by 1.5% in 2010, supported by strong growth in Germany. Growth in China and India will be around 12% and 9% respectively in 2010 – emerging market growth is strong and providing export growth to developed economes. China has raised interest rates and tightened banks' reserve requirements, while India has also raised rates. The world economy is expected to grow by 4.6% in 2010, but only 2% in 2011.

3.3 A paper on market events and future prospects, written by the Independent Adviser, is attached.

3.4 Table 1 below shows the changes in asset allocation, how asset allocation compares with the benchmark and with the average fund (WM Local Authority average), and how the change in the market value during the quarter is allocated across asset classes. Items marked (*) in columns 4 and 8 cannot be separately analysed, but are included elsewhere. The WM Local Authority average asset allocation indicates little change apart from market movements in equities.

Table 1: Asset Allocation as at 30th September compared to the Benchmark

Market (1)	Market Value 30.09.10 £M (2)	Market Value 30.09.10 % (3)	WM LA Average 30.09.10 % (4)	Fund Benchmark 30.09.10 % (5)	Market Value 30.06.10 £M (6)	Market Value 30.06.10 % (7)	WM LA Average 30.06.10 % (8)
Fixed Interest							
UK Gilts	17.4	3.8	10.6	4.5	17.1	4.0	11.0
Corp.Bonds	25.1	5.5	*	4.5	24.4	5.8	*
IL Gilts	-	-	4.8	-	-	-	4.8
Overseas	0.0	0.0	2.2	-	-	-	1.9
Emerg. Market	8.5	1.9	-	2.0	8.3	2.0	-
Infrastructure	0.9	0.2	-	-	0.8	0.2	-
Secured loans	4.3	0.9	-	2.0	8.5	2.0	-
Credit Opps.	12.0	2.7	-	2.5	11.6	2.7	-
Credit Alpha	12.3	2.7	-	2.5	10.9	2.6	-
Currency Fund	0.7	0.2			1.1	0.3	
Equities							
UK FTSE350	109.1	24.0	30.9	18.5	101.1	23.8	28.8
UK Smaller co's	15.6	3.4	*	4.0	14.5	3.4	*
Overseas	105.9	23.3	34.5	26.5	98.5	23.2	34.3
USA	49.9	11.0	9.7	-	51.8	12.2	11.6
Europe	25.5	5.6	9.4	-	17.6	4.2	9.5
Japan	7.7	1.7	3.5	-	6.9	1.6	4.2
Pacific	9.4	2.1	4.3	-	8.6	2.0	4.3
Other	13.4	2.9	5.9	-	13.6	3.2	6.0
Other							
Property – UK	23.8	5.2	6.2	8.0	22.5	5.3	6.8
Property – Eu.	6.6	1.5	*	*	6.1	1.4	*
Hedge funds	41.1	9.0	2.0	10.0	40.7	9.6	2.6
Private Equity	41.7	9.2	2.8	8.0	38.2	9.0	3.4
GTAA	12.7	2.8	1.3	4.0	9.9	2.3	1.2
Infrastructure	4.6	1.1	*	2.0	5.1	1.2	*
Cash	11.8	2.6	4.0	1.0	5.3	1.2	4.0
Total	**454.1**	**100.0**	**100.0**	**100.0**	**424.6**	**100.0**	**100.0**

3.5 The main changes to the Brent Fund have occurred as a result of market movements, agreed rebalancing and increased exposure to private equity. During the quarter, £3.5m was invested in private equity and £1m in UK property.

Since the end of the quarter there has also been further investment in UK property (£1m) and Infrastructure (£0.8m).

Performance of the Fund

3.6 The independent WM Company measures the returns on the Brent Pension Fund. Table 2 sets out returns for the quarter to 3oth September 2010.

Table 2: Investment Returns in Individual Markets

Investment Category	RETURNS						Benchmark/ Index Description
	Quarter Ending 30.09.10			Year Ended 30.09.10			
	Fund %	Benchmark %	WM Local Auth %	Fund %	Benchmark %	WM Local Auth %	
UK Equities			14.2			13.2	
UK Equities	13.7	13.7		14.0	12.6		FTSE 350
UK Small Caps	10.0	11.6		2.5	-0.6		FTSE Smallcap ex IT
Global Equities	7.7	7.6	8.2	2.1	6.3	7.9	FTSE World 75% Hedge
North America	6.2	5.7	6.2	8.4	11.9	12.1	FTSE USA
Europe	9.5	14.1	12.3	-4.9	1.6	2.9	FTSE Eu Ex UK
UK	15.5	13.7	14.2	8.4	12.6	13.2	FTSE All Share
Japan	3.1	0.5	0.1	7.6	1.2	2.3	FTSE Japan
Pacific (ex Jap)	4.5	14.8	13.6	0.5	17.5	18.2	FTSE Pac. Ex Jap
Emerging	14.9	12.1	12.2	18.0	23.3	21.8	FTSE World (Other)
Fixed Interest							
Total Bonds	4.2	2.6	4.3	9.9	5.7	10.6	Brent benchmark
UK Bonds	3.8	3.6	-	4.2	3.8	-	FTSE UK over 15 years
Index Linked UK	-	-	4.0	-	-	9.7	-
Corp Bonds	5.1	4.8	-	10.4	11.5	-	iBoxx Sterling Non-gilt
Secured Loans	4.5	0.9	-	15.1	3.7	-	3 month LIBOR +3%
Credit Opportunities fund	3.7	1.4	-	11.7	5.7	-	3 month LIBOR+5%
Other							
UK Property FOF	1.9	2.2	2.3	22.1	22.6	17.6	IPD Pooled index
Eu Property FOF	8.0	1.9	-	-7.4	8.0	-	IPD All properties
Hedge Funds	0.9	1.1	2.1	1.0	4.5	6.6	3 month LIBID+4%
Private equity	2.3	0.1	2.7	8.0	0.4	9.9	LIBID 7 Day
Infrastructure	-0.1	1.1	-	-3.0	4.4	-	3 Month LIBID +4%
GTAA	27.8	13.8	-	25.3	11.8	-	FTSE 100
Cash	0.8	0.1	1.5	n/a	2.4	3.0	GPB 7 DAY LIBID
Total	**7.1**	**6.3**	**8.5**	**7.9**	**7.8**	**11.3**	

3.7 Details of individual managers' performance tables are attached in Table 3, which shows three month, one year and longer-term information. Returns for the quarter outperformed the benchmark by 0.8%. Part of the outperformance arose as a result of asset allocation (overweight equites). The main stock selection factors were:-

a) Fixed interest. Both the core and satellite portfolios outperformed. The core portfolio benefitted from falling yields as markets anticipated further quantitative easing. The satellite fund rose in value as markets recoverd confidence in the credit worthiness of companies, and as the manager was able to add value through active trading.

b) GTAA. The manager outperformed sharply as three of the four strategies added value. In equities, additional (long) exposure to UK and short exposure to Japan were helpful. In currencies, the overweight to higher yielding currencies added value, as did the short on the dollar. In bonds, the long positions in Japan and USA, and short in Europe, also helped.

c) Property. In European property, returns were helped by the euro recovering value. The european market has begun to improve, and the manager is looking for new funds to commit cash.

d) Hedge funds. Fauchier continue to struggle as markets are heavily correlated and looking at the benefits of quantitative easing. The manager has reduced their allocation to equity long/short managers (and increased exposure to event driven strategies), but is waiting for fundamentals to reassert themselves.

3.8 Over one year, the Fund outperformed the benchmark by 0.1%. Asset allocation – lower exposure to UK Small companies and overseas equities, higher exposure to bonds and cash (held to fund the Infrastructure mandate) - has been negative. Stock selection added value – UK equities, bonds, GTAA and private added value.

3.9 The relative underperformance of the Brent fund against the WM Local Authority average in Q4 (-1.4%) arises as a result of asset allocation - low exposure to equities / high exposure to alternative investments.

3.10 The Brent fund has underperformed the average local authority fund by 3.4% over one year, mainly because it has had a lower exposure to equities (higher exposure to alternatives – mainly hedge funds and private equity) in a period when equities have performed very strongly. Relative performance has also suffered as a result of reduced returns in global equities.

Actions taken by the Brent In-House UK Equity Manager during the Quarter

3.11 There has been some purchases and sales during this quarter to invest dividends (£0.9m) improve tracking error and invest in private equity.

Purchases

a) Took up rights issues.
b) To reduce tracking error.

Sales

a) Sold stocks to ensure more accurate index tracking or as they left the index (such as Edinburgh Dragon Trust).
b) Sold stocks to fund investment elsewhere or to pay retirement lump sums.

Future Strategy for the UK FTSE350 Index tracking fund

3.12 The strategy is that of tracking the FTSE 350 within 0.5% over the year. Activity during October and November included selling stocks to fund increased exposure to property and infrastructure, and to pay retirement lump sums to staff.

NEW DEVELOPMENTS AND FUTURE INVESTMENT OUTLOOK FOR THE BRENT FUND

3.13 Equity markets rose during October and early November in anticipation (and after) further QE in USA.

3.14 The Henderson Liquid Assets Fund (HLAF), the money market fund used by Henderson, will be managed by DB Advisors (an arm of Deutsche Bank) as from 12th October. The change has been made in response to regulators considering bringing treasury style money market funds within the scope of banking regulations – Henderson is an independent investment manager that does not seek to offer banking type products. The change will have no impact on investment strategy in the short term, but Brent will be notified if DB makes formal proposals for change. DB utilises an extensive range of cash investment instruments and has a strong reputation. Brent had £0.9m invested in HLAF as at 30th September.

3.15 The Local Government Pension Scheme (LGPS) is currently under review by John Hutton, following a long period of rising costs and negative publicity. Two recent announcements have helped funding levels – the switch from RPI to CPI will reduce inflation related payments to pensioners, and the two year pay freeze will reduce the rise in the value of benefits. Hutto's initial findings include a career average scheme (rather than final salary related), higher employee contributions, the exploration of a hybrid defined benefit / defined contribution scheme, and a review of the pension accrual rate (currently one sixtieth per annum). The government has said that it will await Hutton's final proposals, but has announced that it will increase employee contributions on a phased basis from 2012.

3.16 Following the announcement that the head of small companies, Gervais Williams, was leaving Gartmore Investment Management, there have been further announcements of the imminent departure of the leading hedge fund manager and the chief investment officer. The stock market price has dropped sharply.Gartmore has announced that it is conducting a strategic review of the business, and is meeting interested companies with a view to a potential takeover. It is proposed that Brent will continue its existing process, but I will update members at the meeting.

4. FINANCIAL IMPLICATIONS

These are contained within the body of the report.

5. STAFFING IMPLICATIONS

None directly.

6 DIVERSITY IMPLICATIONS

The proposals in this report have been subject to screening and officers believe that there are no diversity implications arising from it.

7 LEGAL IMPLICATIONS

There are no legal implications arising from the report.

8. BACKGROUND INFORMATION

Henderson Investors – September 2010 quarter report

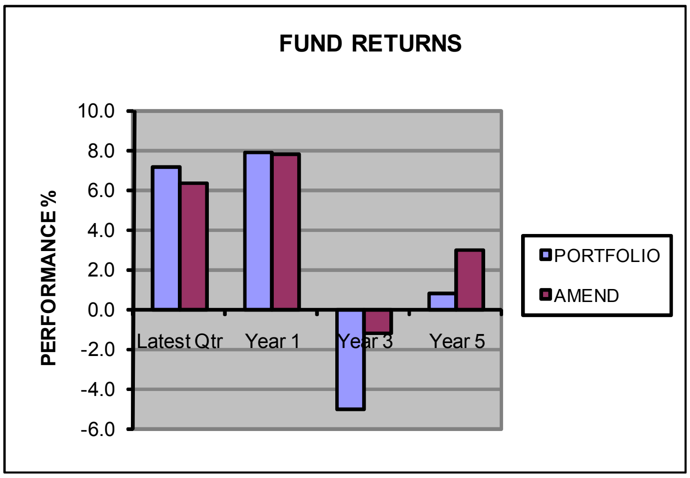
Persons wishing to discuss the above should contact the Exchequer and Investment Section, Finance and Corporate Resources, 020 8937 1472/1473 at Brent Town Hall.

CLIVE HEAPHY
Director of Finance and Corporate Services

PERFORMANCE FOR INDIVIDUAL PORTFOLIOS 30th SEPTEMBER 2010

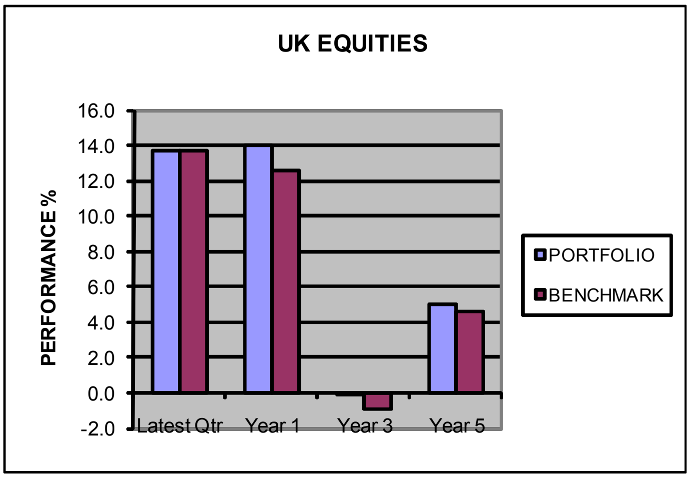
FUND RETURNS

	PORTFOLIO	BENCHMARK
Latest Qtr	7.1	6.3
Year 1	7.9	7.8
Year 3	-5.0	-1.2
Year 5	0.8	3.0



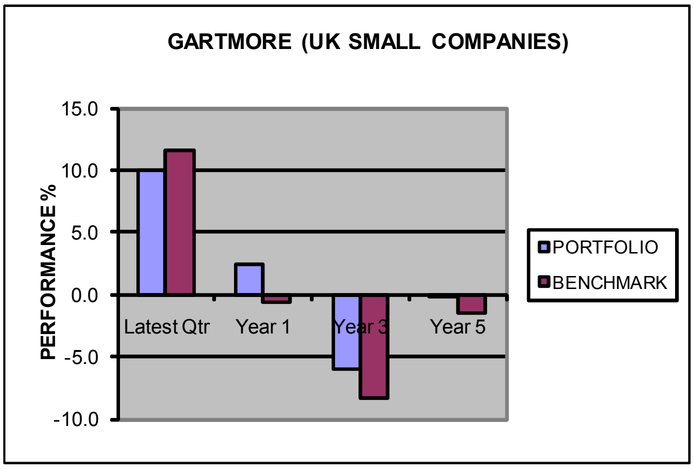
UK EQUITIES

	PORTFOLIO	BENCHMARK
Latest Qtr	13.7	13.7
Year 1	14.0	12.6
Year 3	-0.1	-0.9
Year 5	5.0	4.6



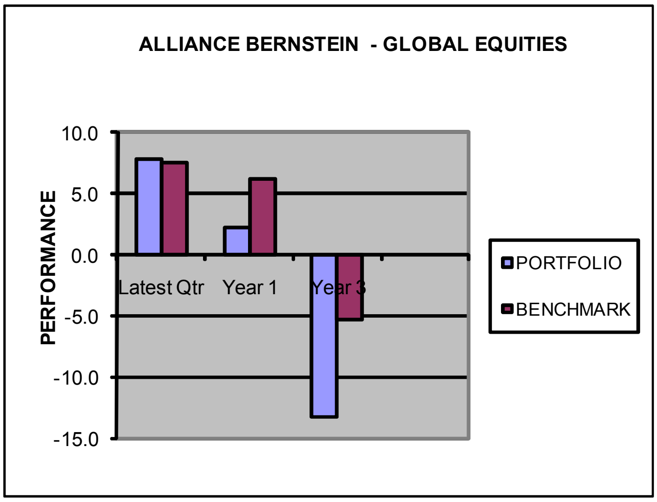
GARTMORE (UK SMALL COMPANIES)

	PORTFOLIO	BENCHMARK
Latest Qtr	10.0	11.6
Year 1	2.5	-0.6
Year 3	-6.0	-8.4
Year 5	-0.2	-1.5



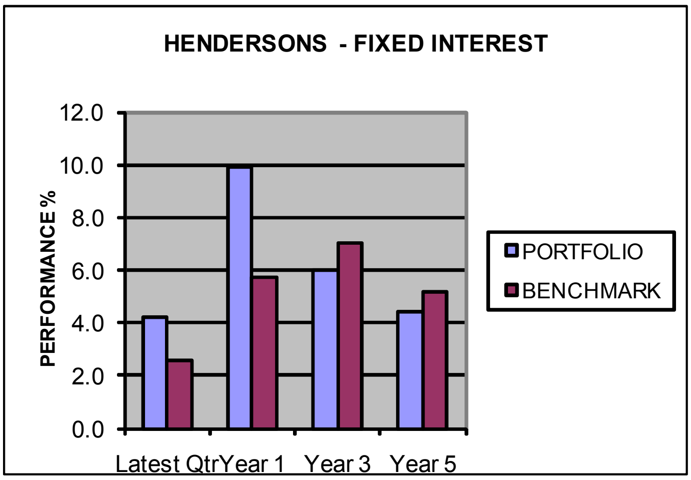
ALLIANCE BERNSTEIN - GLOBAL EQUITIES

	PORTFOLIO	BENCHMARK
Latest Qtr	7.8	7.6
Year 1	2.3	6.3
Year 3	-13.2	-5.2



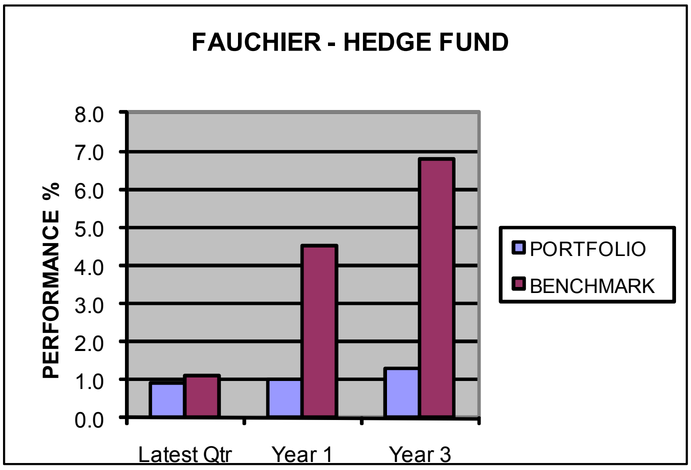
HENDERSONS - FIXED INTEREST

	PORTFOLIO	BENCHMARK
Latest Qtr	4.2	2.6
Year 1	9.9	5.7
Year 3	6.0	7.0
Year 5	4.4	5.2



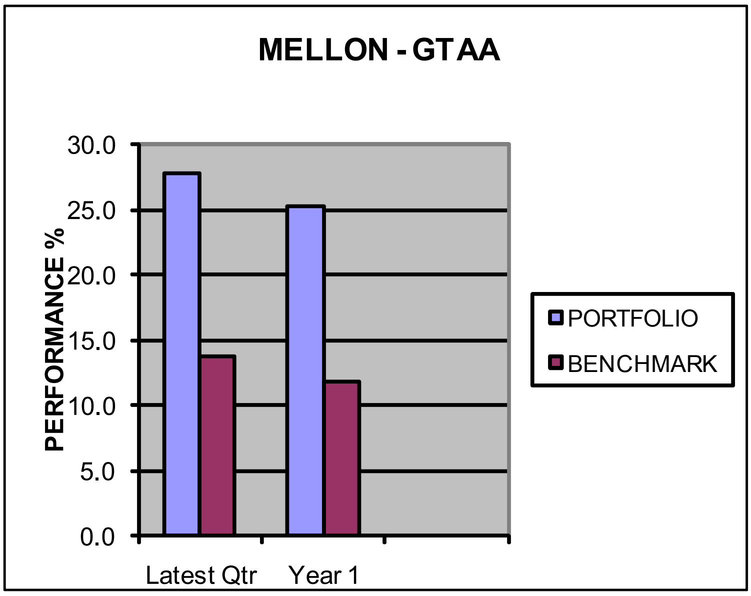
FAUCHIER - HEDGE FUND

	PORTFOLIO	BENCHMARK
Latest Qtr	0.9	1.1
Year 1	1.0	4.5
Year 3	1.3	6.8



MELLON - GTAA

	PORTFOLIO	BENCHMARK
Latest Qtr	27.8	13.8
Year 1	25.3	11.8



Report from the Independent Adviser

Investment Report for the Quarter ended 30th September 2010

Market Commentary

Index returns expressed in sterling

	Indices	Q/E 30.09.10
		%
Equities		
Asia/Pacific	FTSE Developed Asia Pacific (ex Japan)	15.0
UK	FTSE All Share	13.6
Europe	FTSE Developed Europe (ex UK)	13.4
Emerging Markets	MSCI Emerging Markets Free	12.2
North America	FTSE North America	5.8
Japan	FTSE Developed Japan	0.1
Fixed Interest		
Corporate Bonds	Merrill Lynch Sterling – Non Gilts All Stocks	4.8
UK ILGs	FTSE British Government IL Over 5 years	4.1
UK Gilts	FTSE British Government All Stocks	3.6
Property	IPD	Not available
Cash	Merrill Lynch LIBOR 3 Month	0.1

Currency Movements for the quarter ended 30th September2010

Currency	30th June 2010	30th September 2010	Change %
USD/GBP	1.496	1.576	5.3
EUR/GBP	1.221	1.154	-5.5
USD/EUR	1.225	1.365	11.5
YEN/USD	88.490	83.450	-5.6

In strict contrast to the markedly negative equity returns of the previous quarter, those for the reported quarter brought some welcome cheer to stockholders in all equity markets. Highest on the leader board was the 15.0% return from the Asia/Pacific region – scarcely surprising in view of the buoyant underlying economic growth of its member nations. It was heartening to see that second was the UK, up a robust 13.6%. A strong turnaround from its 11.8% negative return in the previous quarter. Both Europe (+13.4%) and Emerging Markets (+12.2%) staged powerful recoveries despite the former's problems with the deficits of Greece and Ireland. The return from the USA (+5.8%) would most probably have been higher, but for the deteriorating economic conditions besetting President Obama's Democratic Party. Japan, as so often in the past, was at the bottom of the pack, recording a minuscule 0.1% return, a reflection of the political squabbling and power struggle for the post of prime minister together with the increasing lack of investor patience.

All three sub sectors of Fixed Interest were in positive territory, but could in no way be compared with the returns from equities. The strongest return came from Corporate Bonds (+4.8%) with the obvious attraction of their high yields. Both Index Linked Gilts (+4.1%) and pure Gilts (+3.6%) produced very creditable returns, boosted by safe haven investors. As a consequence the yields on these sub sectors of Fixed Interest were driven down to levels which could not have been envisaged earlier in the year.

In general market sentiment improved over the quarter due to the following beneficial influences:-

- The historically very low returns on cash deposits caused both institutional and private investors (some of whom were holding much higher levels of liquidity than usual) to take advantage of attractive equity valuations, particularly those with a high yield and a substantial proportion of corporate earnings emanating from overseas. This applied not just to UK investors, but also international investors as they sought to further increase globalisation in their portfolios.
- A sharp upturn in the use of shipping container transport. This is usually a reasonably reliable barometer of the state of the global economy. This was also borne out by the World Trade Organisation reporting that the value of world trade in the first half of 2010 expanded at a substantial annualised rate of 25.0%.
- Fears of rising inflation levels diminished as the measures taken by both governments and central banks appeared to introduce greater control. Worryingly, however, the Bank of England proved an exception with inflation levels well over the government’s 2.0% target.
- As the end of the quarter approached and it seemed that equities would most likely achieve strong returns, this caused institutional investors to be involved in a certain amount of “window dressing”, not wishing to be seen to be holding too high levels of cash at the quarter end.
- Corporate earnings and dividends were mostly better than investment analysts had been expecting. However, accompanying statements were generally cautiously optimistic.
- Across the globe most governments and central banks maintained their interest rates at extremely low levels, particularly those nations in the Western Hemisphere. However, certain Eastern Hemisphere central banks actually increased their rates in order both to guard against their rapidly growing economies becoming overheated and also to pre-empt the likelihood of rising inflation. Of course, the paradox for those countries with fast growing economies was to protect their vital export trade by attempting to stop their currencies from surging. Indeed, in that regard, it is almost as if respective central banks vied with each other to keep currency levels low in order for their exports to remain competitive in the international market place.
- The perception that governments were attempting to better control their respective banking systems and to make practices far more transparent with a higher degree of regulation.
- The continuance of much needed deleveraging both amongst the banks and industry as a whole.
- Tentative signs that the world’s financial systems were becoming more liquid which should be a stimulus to improving bank lending.
- And finally, the most important , very few signs amongst the industrialised nations of their economic activity falling back into recession (with the obvious exception of some of the smaller and highly indebted Eurozone countries). Whilst most countries managed to increase their rates of GDP growth the growth rates of some of the Western Hemisphere countries were anaemic indeed.

Within the leading global economies the principal factors affecting the course of equities, fixed interest and other asset classes were as below:-

- In the UK, the coalition government experienced a surprisingly calm honeymoon period as it began its programme to reduce the fiscal deficit. Company results and exports were better than expected. There was a re-emergence of merger and acquisition activity together with an increase in buyouts within private equity, but residential property prices weakened.
- In the USA, President Obama came under constant attack for the Democratic Party's economic policies which caused consumers' morale to fall as they worried both about job security and collapsing house prices. The imminence of the mid term elections on November 2nd prayed on the White House as there was increasing concern that the Democrats might lose their majority both in the House of Representatives and also in the Senate which would considerably weaken Obama's ability to enact strong legislation.
- In Europe, economic growth continued at two speeds with Germany (the powerhouse of the Eurozone) and the Nordic countries growing rates of GDP relatively strongly whilst Greece, Ireland, Portugal and Spain experienced either very weak economic growth or even recession. Trichet, the head of the European Central Bank, did a creditable job of holding the Eurozone together.
- In Asia/Pacific and Emerging Markets, rates of GDP growth continued at a generally very strong pace, headed inevitably by China. Considerable inter regional trade took place with less of a reliance on exports to the USA and Europe. There was evidence that China is at last prepared to bend to international pressure in order to revalue its currency the renminbi. It is attempting to effect this without too much loss of face. The Australian economy continued to be strong on the back of its mineral wealth. It even had to increase interest rates to pre-empt a rise in inflation.
- In Japan, it came as little surprise that the economy continued to be adversely affected by its deflationary past. Furthermore, politics continued to be an adverse influence with infighting within the elected Democratic Party over the role of prime minister. Neither was Japan's economy helped by the continuing strength of the Yen, particularly against the US dollar. Fundamentally, it would appear that Japan's culture is having difficulty in embracing modern capitalism.

UK

Positive Influences

- August retail sales grew by 2.8% p.a.
- Export volume in the second quarter rose by a substantial 15.5% due to sterling's depreciation.
- The fiscal budget deficit is proving to be lower than expected due to healthy corporate profits translating into higher tax revenue.
- The rate of July's CPI inflation slipped to 3.1 % from June's 3.7%.
- The number of people employed surged by 184,000 to 29.02M in quarter two, the biggest rise since 1989.

Negative Influences

- The Bank of England official estimates of GDP growth were 1.6% in 2010, 2.7% in 2011 and 3.1% in 2012. These were lower rates than the Bank had estimated in May of 1.7%, 3.4% and 3.5% respectively.

- Imports exceeded exports by £13.2B in the quarter to 31st July representing the largest deficit since records began in 1946.
- The purchasing managers' index for the manufacturing sector for August decreased to 54.3 from 56.9 in July.
- In August the stock of unsold houses rose by 41.3% p.a.
- The Bank of England reported that August mortgage approvals fell to 45,000 from July's 47,000.
- On 11th August the Bank of England warned that although inflation will continue to be over target the Bank is unlikely to toughen monetary policy.

USA

Positive Influences

- On 21st September the FED stated that it was "prepared to provide additional accommodation if needed to support the economic recovery". This appeared to be a signal for another programme of quantitative easing.
- The private sector created 235,000 jobs in the quarter to 31st August.
- The Conference Board's confidence index rose to 53.3 in August from 51.0 in July. This was better than economists expected.
- The purchasing managers' index increased to 56.3 in August compared with 55.5 in July.
- The Commerce Department reported that August housing starts rose by 10.5%, a much higher level than expected.
- On 11th August, in a further monetary easing programme, the FED said that it would purchase $18B of Treasury Bonds over the next month.
- Durable goods orders in August rose 2.0% against consensus economists' forecasts for an increase of 1.0%.

Negative Influences

- On 10th August the FED held interest rates and stated that it would continue to hold rates for an extended period. The FED added "the pace of recovery in output and unemployment has slowed in recent months and is likely to be more modest than anticipated in the near term".
- On 3rd September President Obama said "there is no quick fix to the worst recession we've seen since the Great Depression". He added "the economy is moving in a positive direction, jobs are being created, they are just not being created fast enough given the big hole that we've experienced".
- On 8th September the "Beige Book" reported "widespread signs of a deceleration" in growth during August.
- The August unemployment rate inched up to 9.6% (July 9.5%)
- The second quarter's rate of GDP growth was revised down to 1.6% from 2.4%, partly due to a 32.4% p.a. rise in imports, the largest increase for 26 years.
- The ISM index of national services activity decreased to 51.5 in August, down from July's strong showing of 54.3.

Europe

Positive Influences

- 27 member countries of the Basel Committee on Banking Supervision agreed that banks will have to triple core tier one capital ratios from 2% to 7% by the year 2019. This ratio measures the highest quality assets that banks hold against future losses.
- On 7th September the Swiss Franc rose to a record 1.2840 versus the euro.
- On 13th September the European Commission estimated that Eurozone GDP will grow at 1.7% in 2010, up from estimates of only 0.9% in May. This is largely as a result of the second quarter GDP rise of 1.0%. For 2011 the ECB's estimate is 1.4% versus 1.2% earlier.
- Sweden's government estimates that the country's GDP growth rate is set to reach 4.5% in 2010. The Riksbank of Sweden raised interest rates by ¼% to ¾% in the expectation of strong economic growth.
- On 5th August Mr Trichet of the ECB said that at the present time he was sending "absolutely no signal of change in interest rates". On 2nd September Trichet said he expects "positive underlying momentum" in the Eurozone economy and that he ruled out "a double dip back into recession".
- On 25th August Germany's IFO Institute business climate index was the highest since June 2007.
- The Bundesbank estimates German economic growth of 3.0% in 2010 versus its previous estimate of 2.0%. German GDP grew by a robust 2.2% in the second quarter compared with estimates for a rise of 1.3%. This was due to better than expected domestic and foreign demand.
- France's second quarter GDP growth was a better than expected +0.6% due to businesses buying to invest and build up stocks again.
- The Italian Treasury estimates that GDP in 2010 will grow by 1.2% versus its previous estimate of 1.0%. It estimates a growth rate of 1.3% for 2011 against its previous estimate of 1.5%.

Negative Influences

- Germany's leading banks need to raise up to €105B of extra capital under a global regulatory overhaul.
- German orders for July decreased by 2.2% (June +3.6%).
- The Eurozone's composite purchasing managers' index, covering both the manufacturing and service sectors, slipped to 56.1 in August from 56.7 in July. Germany's PMI index was 59.3 for August compared with 59.0 for July, whilst the corresponding figures for France were 59.0 and 59.7 respectively.
- Eurozone inflation for July was 1.7% against 1.4% for June. This increase was partly due to a strong rise in energy prices.
- The Eurozone purchasing managers' index for September shrank to 53.8 from August's 56.2.
- Second quarter GDP returns for some of the weaker Eurozone countries were as follows:-

Portugal	+0.2%
Spain	+0.2%
Greece	-1.5%, its seventh quarterly contraction

- Irelands second quarter GDP fell by 1.2% compared with the first quarter's increase of 2.2%.
- It is officially estimated that the cost of saving the Irish banking system could be as high as £43B which represents more than a third of national income.

Japan

Positive Influences

- On 30th August the Bank of Japan announced an extra ¥10,000B of financing plus a ¥920B package of stimulative measures.
- On 8th September the Yen reached a 15 year high against the US dollar.

Negative Influences

- There was a damaging unsuccessful leadership challenge to the incumbent Democratic Party Prime Minister, Naoto Kan, by his rival Ichiro Ozawa.
- Second quarter GDP was a weak increase of 0.4% p.a., well below the advance of 4.4% p.a. in the first quarter.

Asia/Emerging Markets

Positive Influences

- China's industrial production for August grew by 13.9% p.a. (July +13.4% p.a.) retail sales increased by 18.4% p.a. (July +17.9% p.a.), and purchasing managers' index rose to 51.7 from July's 51.2.
- More recently China more than doubled its holdings of South Korean treasury bonds, in line with it declared policy of investing some of its foreign exchange reserves in currencies other than the US$ and the Euro. China is in the course of displacing Japan as the world's second largest economy.
- China's exports in July grew a prodigious 38.1% p.a. from +43.9% p.a. in June whilst its imports increased by 22.7% in July compared with June's rise of 34.1%.
- India's second quarter GDP recorded a strong growth of 8.8% p.a. (quarter one 8.6% p.a.). India's industrial output for July advanced a marked 13.8% p.a., nearly twice estimates of 7.7% p.a.

Negative Influences

- China's trade surplus for August decreased to $20.0B down from $28.7B as a result of booming imports. China's inflation rate increased to 3.3% in July versus 2.9% in June and compares with a target of 3.0%.
- Julia Gillard was declared Australia's new prime minister forming a centre left labour government. This will be a minority government which could pose problems in voting through essential legislation.

Conclusion

So, whither the stock markets between now and the year end? Certainly a considerable momentum has built up over the reported quarter and investor sentiment has greatly improved. Such a boost to sentiment seems well justified and likely to continue for the following principal reasons:-

- Financial systems, after rigorous purging, now seem to be under much better and more stringent controls and regulations. It appears unlikely that any more large skeletons have yet to fall out of banking cupboards.

- In relation to further recessions, there are reasons to suggest that weaker economies will experience weak rates of GDP growth. This applies especially to the UK and USA. The central banks of these countries have signalled that they are prepared to apply further quantitative easing (QE) by buying up treasury bonds. The weaker economies of the Eurozone may return to negative rates of GDP, for relatively short periods of time. It is no longer considered that higher inflation is an inevitable consequence of Q.E, but this could be wishful thinking.

- The governments of weak economies seem more prepared to grow their way out of recession rather than to inflate their way out.

- Interest rates should continue to remain at their current low levels for some time.

- Purchasing managers' indices have been trending up in most countries.

- Corporate earnings and dividends should continue to be better than expected.

- Markets have yet to fully discount the encouraging upturn in world trade. Indeed, world trade is estimated to grow by 13 ½% in 2010, higher than previously forecast. Not surprisingly, the area of greatest trade growth is expected to be within Asia. Furthermore, the International Monetary Fund is forecasting global GDP growth of 4.6% in 2010, split between 6 ½% for Asia, Emerging Markets and Brazil and 2 ½% average for the Western Hemisphere.

- The recent high levels of mergers and acquisitions, both actual and rumoured, eg BHP Billiton's bid for the Potash Corporation of Canada – also SAB Miller's bid for the Foster Group of Australia and China's alleged interest in United Biscuits here in the UK. These acquisition activities seem likely to accelerate.

- There is evidence that businesses have started to re-invest.

- Cash levels within the investing institutions are higher than normal.

It is an amalgam of all these factors which should be construed bullishly in the market place both in the UK and globally. It seems reasonable to re-iterate the forecast contained in the conclusion of the previous quarter's report - equity returns could be in the high single digit area. However, do not expect the course of markets to be smooth. There will still be periods of fear resulting in high levels of volatility and short term trading. It does seem likely that the optimistic influences mentioned above will hold sway over the negative influences of the severe fiscal deficits in the UK, USA and smaller Eurozone countries, the high rates of unemployment and the collapse of residential property prices in many countries, particularly in the UK and USA.

Comments on the future course of other asset classes are as follows:-

<u>Fixed Interest</u>

With yields on government debt having been driven to such very low levels its seems likely that the sub sector of Fixed Interest will remain flat for quite some time. Also, index linked stocks seem unlikely to make much progress with inflation rates seemingly under control, despite the continuance of quantitative easing programmes. However, corporate bonds would still seem to have further mileage on yield grounds.

Hedge Fund of Funds

Hedge fund of funds should recover from their period of poor performance, especially if market volatility increases together with less correlation between asset classes. These two elements should provide attractive opportunities thereby giving hedge fund of funds the chance of achieving positive absolute return against all market backgrounds.

Private Equity

Private equity should continue to recover from a difficult period as an increasing number of attractive opportunities emerge, in particular, corporate buy outs. Additionally there are attractions within the secondary market.

Property

Property should continue a steady recovery from the deep slump of 2008/9. However, the sub sectors offices, industrial, retail, shopping centres and residential are likely to improve at different rates. The accent on prime properties will continue to be stressed by risk averse investors. There should continue to be a pronounced trend towards globalisation in the property sector, but not towards Southern Europe at this time.

Infrastructure

The outlook for infrastructure appears to be good with an increasing number of opportunities worldwide, especially in the USA and Asia.

Other Alternatives

With regard to the remaining asset classes of Global Tactical Asset Allocation, Currency and Commodities, their results will, as usual, be extremely volatile. The performance attribution of these asset classes will have to be judged over the longer term in which these Alternative Classes should provide a pension portfolio both with a reduction in overall portfolio risk and with fundamental diversification.

In sum, it seems reasonable to predict that:-

There may be no double dip recession in either the UK or the USA.
The Eurozone is most unlikely to break up.
The worst of the banking crisis is probably over.Emerging markets and Asian markets generally will continue to outperform their Western counterparts.
Equities will continue to outperform Fixed Interest.

It follows that far sighted pension funds would be well advised to further embrace globalisation. And not just for equities and fixed interest, but also for most other asset classes be they property, private equity, hedge fund of funds or infrastructure. It goes without saying that GTAA, currencies and commodities are inherently global.

If the above forecasts are proved to be wrong it will most likely due to the following:- fiscal deficits take longer to reduce than expected; consumer spending stagnates in part due to the high rates of unemployment and the collapse of residential property; the state of the US economy deteriorates due to political impasse; or the strategy of

governments to manipulate their currencies lower in order to increase exports deteriorates into a competitive backfire.
Valentine Furniss

Investment Report for the Month of October 2010

	Indices	m/ e 31.10.10
		%
Equities		
Europe	FTSE Developed Europe (ex UK)	3.1
UK	FTSE All Share	2.5
North America	FTSE North America	2.3
Emerging Markets	MSCI Emerging Markets Free	1.4
Asia/Pacific	FTSE Developed Asia Pacific (ex Japan)	0.7
Japan	FTSE Developed Japan	0.4
Fixed Interest		
Corporate Bonds	Merrill Lynch Sterling – Non Gilts All Stocks	-0.4
UK Gilts	FTSE British Government All Stocks	-1.4
UK ILGilts	FTSE British Government IL Over 5 years	-1.6
Property	IPD	N/a
Cash	Merrill Lynch LIBOR 3 Month	0.1

Currency movements for month ended 31st October 2010

Currency	30th September 2010	31st October 2010	Change %
USD/GBP	1.576	1.599	+1.5
EUR/GBP	1.154	1.150	-0.3
USD/EUR	1.365	1.390	+1.8
YEN/USD	83.540	80.550	-3.6

Equity returns for the month of October continued their positive momentum from the quarter ended 30th September 2010. These returns were led by Europe (+3.1%) on the perception that the worst of the financial crises were over amongst the weaker economies of the Eurozone, particularly Greece, Ireland, Portugal and Spain. Next came the UK returning +2.5% on the perception that the government coalition was, not only holding together, but continuing to cope adequately with the problems surrounding the deep seated financial deficit. The USA recorded a 2.3% return despite the anxieties created by the imminence of the Mid Term Elections on 2nd November with the likelihood of a pronounced swing to the Republicans, particularly in the House of Representatives. The US market was also spurred by the thought that the Federal Reserve Board would almost certainly have to instigate a further tranche of quantitative easing which was assumed to be beneficial to equities. The 1.4% return from Emerging Markets resulted from the continuing popularity of this asset class, based on the presumption that the constituent countries would continue to experience strong rates of GDP growth. Asia/Pacific (+0.7%) was more subdued than usual, but still positive. In any event this region was due a pause for breath following the heady returns already achieved. And last, but definitely least, was Japan (+0.4%). As so often in the past, Japan was the laggard on the equity leader board as investors appeared to run out of patience, particularly with regard to the lack of firm government policies with which to avoid slipping back into deflation which has bedevilled this country for so long.

With regard to Fixed Interest all the principal sub sectors produced distinctly dull negative returns as investors became apprehensive concerning further central banks' monetary manoeuvring with those of the weaker economies appearing to be running out of effective options for the resuscitation of their respective economies. The Merrill Lynch £ Non Gilts All Stocks (-0.4%) representing corporate bonds demonstrated investor apprehension that, after a strong run, there might be a degree of profit taking. Gilts (-1.4%) reflected the fact that many investors now feel that yields are low enough and therefore there is little more to go for by way of return. Inflation linked gilts (-1.6%) performed poorly, but this was scarcely surprising as they have hitherto experienced reasonable returns and it is now felt by many investors that governments and central banks have a greater control of inflation than in the past. Thus reducing the attraction of this asset class.

The IPD UK Property return is not available for October, but the return for the quarter ended 30th September 2010 is now available and was 2.3% which should be seen as respectable in the circumstances as there was still apprehension within the sector as property continued to recover, albeit at a somewhat pedestrian pace, from the acute down cycle caused by the sub prime debacle and its resultant chaos in the financial system.

The main feature of the currency movements table was the continuing strength of the Yen against the US dollar to a near record level of ¥80.550

During October general factors to affect the course of stock markets were as below:-

- The International Monetary Fund estimates that the global economy will advance by 4.8% in 2010 and by 4.2% in 2011.
- The World Steel Association estimates that global consumption of steel in 2010 will increase by a record 13.1%.
- On 13th October gold reached a record price of US$1,372 per Troy ounce.
- Currency rhetoric continued apace as the central banks of the principal industrialised nations manoeuvred to expand their vital export trade. On that score China remains somewhat of an enigma much to the chagrin of the USA. The obvious risk is that the weakness of the US$, the world's largest reserve currency, could have a destabilising effect on the world economy.

During October the principal events and macro economic data within the regions were as follows:-

UK

- The much awaited Comprehensive Spending Review was duly announced by the Government. As expected, the contents of this review made it quite clear that the UK population would suffer from harsh medicine for some four years in order to reduce the country's fiscal deficit. It was also clear that no family or individual would be untouched by the tough measures. Furthermore the Government emphasised that the country remained very reliant on private sector growth.
- Third quarter GDP grew by 0.8% (quarter two 1.2%). This was double the consensus of economists' estimates. This caused the rating agency Standard & Poors to revise its outlook on the UK's AAA rating to stable from negative. The GDP growth rate between April and September was the strongest for 10 years. Optimistically, the Chancellor of the Exchequer stated "although global economic conditions remain choppy, a steady recovery is under way".

- George Osborne, in an attempt to bolster the national exchequer funds, is to instigate a privatisation programme of the likes of the Royal Mint, the National Air Traffic Service and the Dartford Crossing.
- September retail sales fell by 0.2% versus an estimate of +0.4%.
- The purchasing managers' index for services increased to 53.2 in October from 52.8 in September whilst the corresponding index for manufacturing grew to 55.0 in October from 53.5 in September.
- The government announced that 490,000 public sector employees were to go over the next four years.
- The Office for National Statistics reported that the trade deficit for August reduced to £8.2B from £8.7B in July.
- On 12th October it was confirmed that pensioners would suffer from the switch to the inflation measure using the Consumer Price Index instead of the Retail Price Index.

USA

- GDP for the third quarter of 2010 grew at an annualised rate of 2.0%.
- September new home sales were up 6.6%.
- Durable goods orders for September rose by 3.3%. This was better than expected due to a surge in aircraft bookings.
- On 20th October the US$ fell to a 15 year low of ¥80.83 against the yen.
- In September industrial production unexpectedly fell by 0.2%.
- In October new claims for unemployment benefit rose 13,000 to 462,000.
- On 13th October the Commerce Department reported that the deficit in goods and services for September had widened by 8.7% to $46.3B.
- The Institute of Supply Management's index of non manufacturing activity rose to 54.3 in October from 53.2 in September.
- The minutes of the Federal Reserve Board meeting on 21st September showed that Bernanke has a consensus for increasing quantitative easing.
- 95,000 jobs were lost in September.
- September factory goods orders increased by 2.1%.
- Next week is a crucial one for the US economy. On 2nd November the much debated results of the Mid Term elections will be known and the extent to which the Republicans, particularly its right wing splinter group, will have affected the Democrats and the balance of power at the White House. On the 3rd November Ben Bernanke at the Federal Reserve Board will have to disclose his economic plan and whether or not to introduce another bout of quantitative easing. On 5th November the monthly jobs report will be issued.

Europe

- On 26th October the Riksbank of Sweden raised interest rates by ¼% to 1.0%.
- German industrial orders in August rose by 3.4% (July -1.6%) which was much better than expected.

Japan

- Industrial production fell by a worse than expected 1.9% in September, its fourth consecutive monthly decline.
- CPI inflation in September dropped by 1.1%.

- On 5th October the Bank of Japan introduced a package dubbed “comprehensive monetary easing” whereby it intends to hold its interest rate at virtually zero until deflation is seen to be defeated. It also intends to buy ¥500B of financial assets.

Asia/Pacific

- China’s rate of CPI inflation inched up to 3.6% in September from 3.5% in August. This compares with the government’s target of 3.0%.
- China’s GDP for the third quarter of 2010 increased at 9.6% p.a., marginally lower than the second quarter 10.3% p.a.
- On 19th October, the People’s Bank of China raised interest rates by ¼% taking the one year deposit rates to 2.5% and the one year lending rates to 5.6%. this was the first increase for almost three years.
- China’s foreign exchange reserves in quarter three 2010 increased by a record $194B to a prodigious US $2650B.
- China’s purchasing managers’ index advanced t 54.7 in October from 53.8 in September.
- On 5th October, the Reserve Bank of Australia left interest rates unchanged at 4 ½% against consensus estimates for a ¼% rise.
- In August and September Australia created 112,000 new jobs with the unemployment rate at 5.1%, nearly half the level of the US and parts of the Eurozone.

Conclusion

Although this report is for the month of October it is being written on 5th November. So, by way of addendum we now know two important market influences both from the USA. Firstly, in the Mid Term elections on 2nd November the Republican Party trounced the Democratic Party in the House of Representatives by winning 239 seats to the Democrats’ 185 seats. And in the Senate the Democrats managed to hang on by 51 seats to the Republicans’ 46 seats. This represented a clear upset for President Obama which may well cause a gridlock in legislation. However, the US stock market has reacted surprisingly well . The second influential event was the announcement by the Federal Reserve Board that it is to introduce an additional quantitative easing programme of $600B with which, between now and mid 2011, it will buy US Treasury Stock. This announcement came much as expected and, here again, has been surprisingly well received by investors both in the USA and globally.

In sum, the events and macro economic data of October, do not have a material effect on the forecasts and caveats contained in the conclusion of the report for the quarter ended 30th September 2010.

Valentine Furniss
5th November 2010

BRENT COUNCIL	**Pension Fund Sub Committee** 30 November 2010 **Report from the Director of Finance and Corporate Services**
	Wards Affected: ALL

Fauchier Partners – proposal to join the Jubilee Special Situations Fund

1 Summary

1.1 This report examines a proposal from Fauchier Partners that the Brent Pension Fund invests in the Jubilee Special Situations Fund.

2 Recommendations

2.1 Members are asked to agree to invest 2% of the Fund (£9m) in the Jubilee Special Situations Fund, taking the money from existing investment in the Jubilee Absolute Return Fund.

3.0 Detail

3.1 Currently, Brent has committed 10% of the Brent Pension Fund to the Jubilee Absolute Return Fund (JARF) managed by Fauchier Partners. The initial investment (£18m) was made in March 2005, with a further £16m in 2009. The investment is currently valued at £41m. Apart from September / October 2008, JARF has delivered steady returns of 2.3% above LIBOR – below the 4% target, but above equity returns in the same period. JARF invests in a number of strategies and managers (around 30).

3.2 The credit related crisis since 2007 has highlighted a number of investment opportunities where companies have defaulted on debt, or are in financial or operational difficulties, or are seeking new investment capital, or whose bonds are trading at distressed prices in the market. In these situations, specialist managers can work with management / other interested parties to realise value for investors. For example, managers can help companies go private, or facilitate takeovers or restructurings.

3.3 Such distressed credit opportunities have arisen in past cycles. For example, Fauchier report that in the 3 years following the WorldCom default in 2002, their specialist credit managers generated an average compound return of 19% per annum. Fauchier believe that there will be increasing opportunities over the next four years as leveraged and high yield loans mature and need to be refinanced. Further, skilled managers can control the process by driving restructurings and being active shareholders. The more stringent rules surrounding bank trading (the Volcker rules in USA) may hamper banks from participating in the purchase of securities.

3.4 Fauchier have suggested that Brent invest in their Jubilee Special Situations Fund, both to improve returns and to increase diversification. The Fund will invest with 15 top quality managers chosen on the basis of their research, sourcing of opportunities, ability to identify undervalued situations, knowledge of processes and experience of driving change. The main opportunities are arising in USA and Asia, but not much in Europe. Fauchier have met all the managers, keep them under regular review (weekly information), and have known them for some time (at least 18 months). Within Fauchier, the process will be controlled by the Investment Committee and two experienced analysts. The processes within Fauchier should allow managers to benefit from opportunities while maintaining downside protection. The new Fund will be around \$220m, and Fauchier will commit \$30m of its own resources (including individual investments).

3.5 However, there are additional risks attached to investment in the Special Situations Fund. These include:-

a) The Fund was originally launched in 2007, just before the credit crisis broke, and did badly. The investments made were more similar to private equity than hedge fund investments. The existing underperforming assets have been 'side-pocketed', so that they are allocated to existing investors rather than new investors. The restructured Fund will be more within the hedge fund area of competence.
b) The situations in which the Fund will exist are more risky and volatile than the average in JARF, which are spread across a number of different strategies. However, distressed debt investment is expected to be less volatile and less risky than equity investment – distressed debt has an annual volatility of around 7%, JARF below 6%, but equities around 15% per annum.
c) If required, there is a longer notice period to exit the Fund. There is a one year lock up period, thereafter investors can exit quarterly after giving 120 business days notice.

3.6 Fauchier are keen that Brent join the Special Situations Fund, and have agreed that Brent will pay a similar fee to that paid in the JARF. It is recommended that Brent invest 2% of the overall Brent Fund in the new Special Situations Fund (around £9m), taking the money from the existing JARF.

4.0 Financial Implications

4.1 These are outlined within the report.

5.0 Staffing Implications

5.1 There are no staffing implications.

6.0 Legal Implications

6.1 There are no legal implications.

7.0 Diversity Implications

7.1 The proposals in this report have been subject to screening and officers believe that there are no diversity implications.

8.0 Background Information

Paper from Fauchier Partners on the Special Situations Fund – November 2010.

Contact Officers

Martin Spriggs – Head of Exchequer and Investment
Brent Town Hall, Tel: 020 8937 1472

Clive Heaphy
Director of Finance and Corporate Services

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Pension Fund Sub Committee
30 November 2010

Report from the Director of
Finance and Corporate Services

Wards Affected:
ALL

Brent Pension Fund – socially responsible investment

1. SUMMARY

1.1 This report reviews Socially Responsible Investment (SRI) policies for the Brent Pension Fund.

2. RECOMMENDATIONS

2.1 Members are asked to confirm their existing investment policies as set out in paragraph 3.3 of this report and in the Statement of Investment Principles.

3 DETAIL

Background – Investment in tobacco

3.1 The Health Partnerships Overview and Scrutiny Committee met on 14th October and made a recommendation to the Pension Fund Sub Committee as follows:-

'The Health Partnerships Overview and Scrutiny Committee recommends that the Brent Pension Fund Sub Committee reconsiders the investments that Brent Council has in tobacco firms. The overview and scrutiny committee does not believe that the council should be investing pension fund money in companies that make profits at the expense of peoples' health and that it contradicts the council's work to promote tobacco control and smoking cessation. The committee is encouraged that other council's, such as Harrow, have taken a decision to disinvest from these firms and hopes that the council can follow their lead, especially as Brent is launching its Tobacco Control Strategy on 29th November.'

3.2 The Chief Executive, Gareth Daniel, has also received a letter from NHS Brent urging the reconsideration of investment in tobacco stocks.

Background – Corporate governance and SRI

3.3 The background to the development of sub committee policies on corporate governance and SRI has been controversial. In order to confirm that the management of the pension fund was primarily concerned with generating the best investment returns within acceptable risks, the Council meeting of 13th February 1996 agreed that:-

'The council re-confirms its policy of non-political or administrative interference with the investment manager's investment decisions or involvement with companies in which the fund managers have acquired shares on behalf of the fund.'

In other words, the fund managers will take investment decisions on the basis of the best interests of the Fund, which is held for the best interest of beneficiaries.

3.4 The key background to the council's decision were poor experiences in the 1980's and the principles set out in the Cowan vs Scargill judgement in 1985 (the Megarry judgement). These included:-

a) Trustees are under a duty to exercise their powers in the best interests of the present and future beneficiaries. The best interests will usually be financial interests, unless the trust is a charitable foundation with a particular moral outlook.

b) Trustees must put aside their own personal interests and views and not exercise their powers for any hidden motive.

c) Trustees must take such care as would the 'ordinary prudent person'.

d) Trustees must consider the need to diversify the investments.

3.5 As part of the adoption of the Statement of Investment Principles (SIP) in 2000, the Sub Committee agreed to adopt the 1998 Combined Code on Corporate Governance and to engage with UK companies on corporate governance and SRI issues. The sub committee agreed that soundly managed companies were more likely to comply with best practice in corporate governance and to consider long-term and employment / environmental / sustainable issues (SRI issues) as part of their planning process. As well as voting at Annual General Meetings and Extraordinary General Meetings to support sound governance practices, the Fund joined the Local Authority Pension Fund Forum (LAPFF) to engage with companies and research SRI issues using Pensions Investment Research Consultants (PIRC). The LAPFF has a membership of forty nine local authority funds managing around £80b, giving it a powerful voice in engaging with companies and other relevant groups such as the Association of British Insurers and the Fund Managers Association. The LAPFF has engaged and reported on such issues as the environment, child labour and corporate governance. It was felt that one fund alone had neither the expertise nor the economic weight to influence large companies.

3.6 It has become apparent that the number of SRI mandates in local authority funds has reduced as performance targets have not been met. Investment performance is difficult, and it has been accepted that allowing managers wide discretion should encourage improved performance. However, many funds have integrated SRI principles into their investment agreements to ensure that long-term environmental, social and governmental issues are addressed. There has been support for this approach from the United Nations sponsored Freshfields, Bruckhaus, Deringer opinion that 'integrating ESG (environmental, social and corporate governance) considerations into an investment analysis so as to more reliably predict financial performance is clearly permissible and is arguably required in all jurisdictions.'

Doubt has been cast on the validity of the opinion in the light of the Megarry judgement, but it is apparent that consideration of SRI issues can improve investment analysis. In particular, the risks involved in a large weighting to oil stocks were shown in the recent performance of BP shares when their oil rig exploded in the Gulf of Mexico. However, the questions here are more financial than ethical – similar questions have been raised with AllianceBernstein over their exposure to financial stocks in 2008.

3.7 Other organisations contact Brent Council periodically to raise other SRI issues. In particular, the Campaign Against the Arms Trade (CATT) has previously asked for details of investment in companies producing weapons. Other areas could include alcohol, oil, drug testing, foreign regimes, investment only in UK etc. These could be very subjective areas.

3.8 At their meeting on 20th February 2008, the Sub Committee reconfirmed its policy of non-political or administrative interference with managers' investment decisions. I attach the SIP as Appendix 1. Paragraph 35 sets out policy with regard to Corporate Governance and Socially Responsible Investment.

3.9 Investment in tobacco companies has been highly successful over the years. At present, the Fund invests in two UK tobacco companies – the value of the investment is around £2.5m (though this will reduce as UK equity exposure is reduced as part of the change to asset allocation agreed on September 29th 2010).

3.10 Contrary to the Health Partnerships Overview and Scrutiny Committee assertion that Harrow has disinvested from tobacco stocks, no such action has been taken. Investments continue to be made through pooled funds, with no ethical constraints on managers' activities. Like Brent, Harrow is a member of LAPFF. Officers at Harrow have committed to report on ESG issues in 2011.

3.11 I have circulated other London Boroughs to ascertain their approaches, and have received replies from fourteen. From those that have replied, it appears that most take a similar approach to that followed by Brent – that the fund should be invested in the best financial interests of the members, but that managers should take ESG (SRI) issues into account in their screening of stocks and engage with companies. As with Brent, some of the boroughs used LAPFF to research ESG issues and engage with companies. In most cases, managers are not restricted in their choice of stocks. Two of the boroughs that replied were prepared to exclude 'unethical' stocks, or would encourage their managers to exclude, but either with no loss of performance or only after considering the impact on performance.

Options for action

3.11 An option might be for the UK in-house fund to track the FTSE4Good UK index, which excludes such sectors as manufacturers of nuclear weapon components, tobacco and manufacturers of weapon systems. The index is restricted to the largest 50 stocks that comply with criteria, whereas the Brent Fund currently tracks the FTSE350.

3.12 However, it is recommended that no further action is taken for the reasons given in paragraphs 3.3 – 3.9 and that members confirm their previous policy.

4. FINANCIAL IMPLICATIONS

These have been covered within the report.

5 DIVERSITY IMPLICATIONS

The proposals in this report have been subject to screening and officers believe that there are no diversity implications arising from it.

6 STAFFING IMPLICATIONS

None

7 LEGAL IMPLICATIONS

7.1 In the case of *Cowan v Scargill and Others [1985] Ch. 270*, Vice Chancellor Sir Robert Megarry laid down a number of principles, which include the following:

(1) The duty of trustees to exercise their powers in the best interests of the present and future beneficiaries of the trust and this duty towards their beneficiaries is paramount.
(2) In considering what investments to make, trustees must put on one side their own personal interests and views.
(3) The benefit of the beneficiaries which a trustee must make his paramount concern does not necessarily mean solely their financial benefit. However, the Judge added that under a trust for the provision of financial benefits, the burden would rest heavily on the trustee who asserts that it is for the benefit of the beneficiaries as whole to receive less by reason of the exclusion of some of the possibly more profitable forms of investment. The Judge said that such circumstances would be rare and if such circumstances did not arise, the paramount duty of the trustee would normally be to provide the greatest financial benefit for the present and future beneficiaries.
(4) The required standard required of a trustee in exercising his powers of investment is that he must take such care as an ordinary prudent man would take if he were minded to make an investment for the benefit of other people for whom he felt morally bound to provide. This includes the duty to take professional advice on matters which the trustee does not understand, such as the making of investments and, on receiving that advice, to act with the same degree of prudence.
(5) Trustees have a duty to consider the need for diversification of investments.
(6) The law relating to trusts is applicable to pension funds.

7.2 In the case of *Martin v City of Edinburgh District Council [1988] SLT 329*, Lord Murray ruled that the members of the Council, as trustees, when deciding to withdraw investments from companies which had links with South Africa, had not applied their minds separately and specifically to the question whether the changes in investments would be in the best interests of the beneficiaries of the trusts and that as a result, they were in breach of trust. In this case, the trustees did not consider or take professional advice on whether withdrawing investment from companies which had links with South Africa would be in the interests of the beneficiaries of the trusts. In that case, Lord Murray made the following observation: “I accept that the most profitable investment of funds is one of a number of matters which trustees have to consider. But I cannot conceive that trustees have an unqualified duty … simply to invest trust funds in the most profitable investment available. To accept that without qualification would, in my view, involve substituting the discretion of financial advisors for the discretion of trustees". Lord Murray also said that an individual trustee must recognise that he has certain preferences, commitments or principles but none the less do his best to exercise fair and impartial judgment on the merits of the issue before him.

7.3 In the case of *Bishop of Oxford v (Church Commissioners) [1993] 2 All ER 300*, Vice Chancellor Nicholls accepted that there were at least two exceptions to the duty to maximise financial returns, but they relate mainly to charities. The first exception is where the aims of the charity and objects of investment are in conflict and the second exception is where particular investments detract from the charity's work. In both exceptions, the trustees must weigh the extent of financial loss from offended supporters and the financial risk of exclusion. It is not clear from the case law whether such principles set out in this case apply to all investment trusts such as pension funds.

7.4 There are a number of other requirements laid down by statute. Under section 4 of the Pensions Act 1995 ("the 1995 Act") and subordinate regulations, the trustees' powers of investment must be exercised in a manner calculated to ensure the security, quality, liquidity and profitability of the portfolio as a whole. Under section 4(2)(a) of the 1995 Act, the assets must be invested in the best interests of members and beneficiaries. Under section 2(2)(a) of the 1995 Act, the assets must be properly diversified. Under section 4(7) of the 1995 Act, the trustees must obtain proper advice when preparing their statement of investment principles and under section 36(5) of the 1995 Act, they must act in accordance with those principles as far as practicable.

7.5 There are also statutory requirements laid down under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended) ("the 2009 Regulations"). Under regulation 11 of the 2009 Regulations, a local authority administering a pension fund must formulate a policy for the investment of its fund money, must invest in accordance with its investment policy any fund money that is not needed immediately to make payments from the fund, obtain proper advice at reasonable intervals about its investments and must consider such advice in taking any steps in relation to investments. Subject to these conditions, a local authority may vary its investments. Also under regulation 11, a local authority's investment policy must be formulated with a view to the advisability of investing fund money in a wide variety of investments and to the suitability of particular investments and types of investments.

7.6 Under regulation 12 of the 2009 Regulations, after consultation with such persons as they consider appropriate, a local authority administering pension funds must prepare, maintain and publish a written statement of the principles (known as Statement of Investment Principles – SIP) governing its decisions about the investment of fund money. The SIP must cover the local authority's investment policy on various matters, including the extent, if at all, to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments. The SIP must be reviewed, and if necessary revised, by the local authority from time to and time and in the case of any material change in the local authority's policy on matters referred to in regulation 12(2), before the end of a period of six months beginning with the date of that change. A copy of the Council's SIP is attached as Appendix 1 to this report and the Council's policy on Socially Responsible Investment (SRI) is set out in paragraph 35 thereof.

8 BACKGROUND

Pension Fund Sub Committee – Statement of Investment Principles and Corporate Governance Policy (15th February and 20th June 2000)
Pension Fund Sub Committee – Review of Corporate Governance and Socially Responsible Investment (24th February 2004)
Pension Fund Sub Committee – Brent Pension Fund – Review of the Statement of Investment Principles and Engagement Policy (20th February 2008)
Letter from NHS Brent to the Chief Executive (16th November 2010)

Persons wishing to discuss the above should contact the Martin Spriggs, Exchequer and Investment Section, Brent Financial Services, on 020 8937 1472/74 at Brent Town Hall.

Clive Heaphy
Director of Finance and Corporate Services

LONDON BOROUGH OF BRENT PENSION FUND

STATEMENT OF INVESTMENT PRINCIPLES

Investment Responsibilities

1 Responsibilities are allocated to ensure that the managers are given authority to manage their portfolios, but that there is monitoring and review both at individual portfolio and at total fund levels. The Pension Fund Sub Committee at Brent Council is responsible as administering authority for:

a) Determining the overall investment strategy and strategic asset allocation.

b) Appointing the investment managers, the independent adviser and the actuary.

c) Reviewing investment manager performance and processes regularly.

2 The Chair of the Sub Committee is responsible for ensuring that councillors taking investment decisions are familiar with investment issues and that the Sub Committee has sufficient members for that purpose.

3 The Director of Finance and Corporate Resources at Brent Council is responsible for:

a) Advising and reporting to the Pension Fund Committee.

b) Reviewing the activities of the investment managers on a regular basis.

c) Managing the in-house UK equity portfolio on an index-tracking basis using the FTSE 350 as a benchmark.

d) Keeping the accounts for the Fund and managing cash flow to distribute new money to managers.

4 The investment managers are responsible for:

a) The investment of pension fund assets in accordance with legislation, the Statement of Investment Principles and the individual investment management agreements.

b) Preparation of monthly and quarterly reports detailing activity, investment performance and future strategy, and attendance at the Pension Fund Sub Committee.

5 The actuary is responsible for:

a) Undertaking a triennial revaluation of the assets and liabilities of the fund.

b) Providing advice on the maturity of the fund.

6 The independent adviser is responsible for the provision of advice to the Sub Committee and the Director of Finance and Corporate Resources on all investment issues, in particular asset allocation, new developments and monitoring managers.

The Management of Risk

7 There are three main definitions of risk:

a) severe market decline and funds losing value (absolute risk), as occurred in the period 2000 - 2003.

b) underperformance when compared to a peer group (WM2000, or other local authorities) or relevant stock / bond markets (relative risk).

c) not meeting the liabilities set out in the Local Government Pension Scheme. The Fund had a deficit of £174m when valued in 2004, and` is following a 25 year recovery period.

8 To reduce absolute risk the fund is diversified between managers, asset classes, markets and sectors so that investments are not concentrated in one theme or country / region. Investment managers are also to observe the authority's investment restrictions, which are designed to reduce risk.

9 To add value, the Fund seeks exposure to a variety of risks and associated risk premia. The search for outperformance will, on occasions, involve the risk of underperformance through the adoption of contrarian positions. The extent of any underperformance, through relative risk, has been reduced by diversification and the use of index-tracking with regard to UK equities, index benchmarks and asset allocation ranges in fixed interest.

10 The third definition of risk – failure to meet liabilities – is managed in three ways. First, to enable the administering authority to meet benefit payments, managers may remit payments on a monthly basis when required. This will allow managers to plan any realisation of assets as necessary or, more likely, reinvest income from dividends or interest received. Second, assets and liabilities are valued at least on a triennial basis by an independent actuary (the actuarial valuation) to determine the financial health of the fund. If a deficit is forecast, employers' contributions may be increased to ensure that all liabilities are met. Third, the Brent fund is mature, there being many more pensioners than working members - to the extent that 62% of assets are 'owned' by pensioner liabilities. Therefore there is a need to consider the risks involved in pursuing a long-term equity based strategy when a market correction, and lower dividend payments, could reduce the value of the fund. There is currently a 'mismatch' between the investment of 91% of the fund in real assets (equities, alternative investments and property, that increase with the growth of the economy) and the maturity of the fund. However, this is balanced by; first, the expectation that equities will generate additional returns to facilitate the payment of both pensioners' and active members' benefits; second, it is calculated that contributions from employers and employees will be sufficient to meet benefit payments over at least the next ten years. Managers will be able to continue to reinvest income and change their stock selections without concern about the need to realise assets quickly. However, most assets are liquid and invested in recognised stock exchanges.

11 If the Director of Finance and Corporate Resources becomes concerned that there may be an imminent severe market correction, he is authorised in consultation with the Chair of the Sub Committee and the Independent Adviser, to amend the Fund asset allocation and reduce exposure to those assets classes that may be affected.

Investment Objectives

11 The prime investment objective is to maximise long-term investment returns subject to an appropriate level of risk implicit in the targets set for each investment manager. The current targets are:

a) UK equities – to match the FTSE 350 index.

b) Global equities – to beat the FTSE All World Index by 3% per annum over rolling three-year periods, and to manage currency exposure

c) Fixed interest – to outperform a composite benchmark on 50% of the portfolio:

 25% FTSE Actuaries All Stocks index (UK government bonds)

 25% Merrill Lynch non-gilt index (Corporate bonds)

 by 1% per annum over rolling three year periods, avoiding underperforming the benchmark by 1.5% in any twelve month period.

 To outperform a cash benchmark on 50% of the fund that is managed on a high performance benchmark.

d) UK Small companies – to outperform the FTSE Small cap ex IT index by 2% per annum.

e) Property – UK property to outperform the IPD All properties index by 0.5% per annum over rolling three- year periods, and European property to return 8% per annum.

f) Private equity – to achieve an average return of 10% - 15% per annum over the life of the fund.

g) Hedge funds – to achieve an average return of 9% per annum (LIBOR + 5%).

h) Global Tactical Asset Allocation – to achieve an average return of 20% per annum.

i) Infrastructure – to achieve an average return of 15% per annum, comprising both income and capital growth.

12 The achievement of these targets should attain a minimum real rate of return of 4% - 5% per annum over rolling three-year periods (see asset allocation for returns expected from each market). The 2007 Actuarial Valuation anticipated a return of gilts plus 1.5% per annum, giving a total return of 6.2% per annum.

Asset Allocation

13 Three general points should be noted. First, LGPS regulations require that funds achieve 'proper diversification', which may be considered in terms of ensuring that investments are spread through a number of markets whose movements are not closely correlated. This affords some protection in the event of market corrections, and allows gains from a variety of sources. Second, equities have been the best performing asset class over the very long term, property has performed well over ten years but has tended to be slightly behind equities, whereas bonds and cash have performed less well. Third, exposure to fixed interest gilts and corporate bonds provide income and increased certainty of returns as appropriate for a mature fund. Fourth, exposure to other asset classes adds to diversification and allows additional returns in less well researched markets. The Myners' report advocated that funds should consider all the main asset classes in setting its asset allocation, allowing the Fund access to different risk premia (such as time, currency and different asset valuations).

14 The asset allocation adopted for the fund is as follows:

Asset Class	Prop. of Fund %	Range %	Expected Return p.a %	Benchmark
UK equities	18.5	15-30	6 - 9	FTSE 350
UK Small companies	4	3 - 5	6 - 9	FTSE Smallcap index ex IT
Global equities	26.5	17.5-30	6 - 9	FTSE All World
UK Fixed interest	4.5	2 - 9	4 - 7	FTSE UK All Gilts
Corporate bonds	4.5	1 - 9	4 - 8	Merrill Lynch non-gilt
Secured Loans	4.5	1 - 9	6 – 9	LIBID + 3%
Fixed interest hedge fund	4.5	1 - 9	6 -10	LIBID + 3%
Property	8	5 -10	5 - 9	IPD and absolute return
Private equity	8	2 -10	8 -12	Absolute return
Hedge funds	10	8- 12	6 -12	LIBID + 4%
Infrastructure	2	1 - 7	10 – 20	Absolute return
Global Tactical Asset Allocation	4	2 – 6	15 – 20	FTSE All share
Cash	1	0 - 5	3 - 7	Cash

15 For UK equities, the in-house manager holds stocks in proportion to their weighting in the FTSE 350 Index (known as index tracking, or passive, management). Index tracking has been chosen because the average manager has, in the longer term underperformed the UK index, and in-house management is less expensive than external active management. For overseas equities, the manager has complete discretion in selecting between markets. Active management has been chosen because there are opportunities for the manager to outperform through stock and sector selection. For fixed interest, the manager has discretion to change the asset allocation within ranges, using other bond-like instruments as permitted. Active management has been chosen to allow opportunities for improved performance through stock selection and asset allocation. For property, UK Small companies, hedge funds, currency and private equity, the fund has invested in pooled funds that will allow diversified investment whilst offering the opportunity for additional returns.

16 Asset allocation is reviewed regularly to consider new opportunities that may arise and anticipated returns. The expected returns detailed above are taken from forecasts made by the actuary and investment managers. It is anticipated that equities will not outperform by the same margins seen in the twenty-year period 1980 – 1999, but it is expected that the asset class will outperform gilts. The next major review of asset allocation is expected to be in June 2011, but will be considered at least annually.

Investment Manager Arrangements

17 The review of fund management arrangements undertaken in 1999 concluded that

the optimum investment arrangement is to employ managers implementing a specialist ‘core / satellite’ model. The ‘core’ will be UK equities, managed in-house on an index-tracking basis. The other managers – the ‘satellites’ – will be specialists in their markets concentrating on the outperformance of particular benchmarks. It is expected that this approach will yield the best returns at the lowest cost and the least risk.

18 The current managers are:

UK Equities	In house
Global Equities	AllianceBernstein Institutional Investment Management
Fixed interest	Henderson Global Investors
Property	Aviva Investors
UK Smaller companies	Gartmore Investment Management
Private Equity	London Fund Managers
	Capital Dynamics
Hedge Funds	Fauchier Partners
GTAA	Mellon Global
Infrastructure	Alinda Partners

19 Management fees are calculated on the basis of a percentage of funds under management, rather than a performance basis, with the exception of the fixed interest, private equity, hedge fund and currency managers. This basis has been chosen because basic fees should be sufficient to incentivise managers in traditional areas, but performance fees are felt to be necessary to align interests in other areas.

Investment Restrictions

20 The Local Government Pension Scheme states that the authority shall have regard both to the diversification and the suitability of investments. A number of investment regulations are also applicable to the fund. These were amended in 2003 to allow each fund more discretion over investment policy by allowing a range of limits within an overall ceiling. The Pension Fund Sub Committee has decided that the Brent fund may not:

a) invest more than 10% of the fund in unlisted securities.

b) invest more than 10% of the fund in a single holding (unchanged), or more than 25% of the fund in unit trusts managed by any one body.

c) excluding loans to the government, lend more than 10% of the value of the fund to any one borrower.

d) contribute more than 5% of the fund to any single partnership.

e) contribute more than 15% of the fund to partnerships.

21 The reasons for this approach are:

a) Diversification. The Myners report has highlighted the need to access a wider range of asset classes both to spread risk and add to returns. The main alternative asset classes under consideration by pension funds are private equity, hedge funds, infrastucture and property. The main route for access to private equity and hedge funds is through partnerships (sometimes known as 'fund of funds').

b) The Brent fund has committed 8% of assets to private equity through partnerships, 5% to infrastructure and 10% to hedge funds. This may increase in future as experience of private equity and hedge funds develop.

22 The decision to increase limits will apply for ten years and complies with the new Investment Regulations. However, asset allocation decisions are regularly reviewed and the suitability of the limits will be subject to reconsideration at least every three years as part of the asset allocation review.

23 The authority has also imposed a number of restrictions to reduce risk and to maintain control of fee levels. The managers may not:

a) undertake stocklending arrangements.

b) invest in any in-house fund without prior consent.

c) exceed the limits set out in the asset allocation ranges detailed in the benchmark.

d) borrow.

e) Engage in underwriting or sub-underwriting on behalf of the fund.

f) Enter into soft commission arrangements, by which business is directed to brokers in exchange for other services such as research or systems.

24 Managers may use derivatives to facilitate asset allocation decisions and trading, to obtain exposure to markets / assets, to reduce trading costs, and to protect the value of overseas investments. All open and completed transactions will be included in monthly transactions and quarterly reports.

25 The restrictions are designed to aid transparency, avoid speculative investments, reduce the volatility of returns, and facilitate the realisation of investments. However, research has indicated that indiscriminate restrictions reduce managers opportunities to use skill to add value. On this basis, restrictions are kept to a minimum.

Manager Discretion

26 With the exception of the in-house portfolio, managers are given wide discretion over both stock selection and asset allocation within the restrictions detailed above. This allows clear accountability for decisions. The managers have established procedures to monitor and control risk, and to research market trends.

Monitoring activity and performance – Managers, adviser and trustees

27 Local Government Pension Scheme regulations state that the administering authority. should review, at least every three months, the investments made by managers and should have regard to professional advice. The Myners' review has emphasised the importance of monitoring dealing costs – these will be reviewed with other aspects of investment.

28 WM is an independent performance monitoring agency that measures the performance of the total fund and the individual managers against both the benchmark and peer group funds. Reports are produced quarterly and annually to allow proper consideration of performance over both the short and medium term. If a manager consistently underperforms benchmarks over a ‘substantial’ period (defined as six quarters) a review of the mandate will be considered.

29 The Director of Finance and Corporate Resources monitors managers’ activity on a daily, monthly and quarterly basis, and is in regular contact with investment houses. The Pension Fund Sub Committee receives quarterly reports from the investment managers and the Director of Finance and Corporate Resources detailing activity and investment performance.

30 The Sub Committee will review the performance of the pension fund adviser on a triennial basis, looking at the quality of advice and inputs made.

31 The Sub Committee (trustees) will agree an annual and three year business plan to ensure that all areas of activity, including member training and development, are adequately examined and reviewed. The Sub Committee will review its own performance on an annual basis, looking at the performance of the fund overall and progress against the business plan.

Review of the Implementation of Investment Policy

32 The appointment of the investment managers will be reviewed regularly by the Pension Fund Sub-Committee to consider the desirability of continuing or terminating the appointment. Decisions will be based on monitoring the investment performance and processes at quarterly and other meetings.

33 Amongst the criteria by which managers will be selected are:

a) Investment process, including investment philosophy, research, the asset allocation process, controls on stock selection, and risk controls.

b) Past performance, including spread of results and volatility.

c) Personnel, including levels of experience, staff turnover, and the individual managers offered.

d) Administration, including systems, contacts, references from other customers, and the ability to meet requirements on reporting.

e) Resources, including the number of professionals employed, the number of funds serviced, the number of funds gained or lost over the last 5 years, and the controls on over-rapid growth.

f) Professional judgement.

34 A manager may be replaced if, amongst other things, they fail to meet the investment objectives or it is believed that they are not capable of achieving the performance objectives in the future. Consistent underperformance over six successive quarters will automatically lead to a review of the mandate.

Corporate Governance and Socially Responsible Investment

35 The Pension Fund Investment Sub-Committee has agreed the following policies:

a) A corporate governance policy for UK equities is attached in Appendix 1. The fund will use an agency service (RREV) to support regular voting at Annual and Extraordinary General Meetings.

b) The Global equities manager, AllianceBernstein, will vote on behalf of the fund on corporate governance issues overseas. The manager supports the fundamental principles expressed in the Shareholder Bill of Rights adopted by the Council of Institutional Investors, but also has a close knowledge of overseas companies that will facilitate careful consideration of individual issues. AllianceBernstein has discretion to invest in the best economic interests of the fund. The manager does not make moral judgements on individual stocks, but seeks to avoid companies where ethical or environmental concerns are not fully recognised in the rating of the stock.

c) With regard to socially responsible investment in UK, the fund will use an advisory service (the Local Authority Pension Fund Forum) to facilitate constructive discussions (known as 'engagement') with UK companies where environmental, social or other long-term issues may impact on the value of a company. The fund will continue to hold all relevant stocks within the FTSE 350 but will seek to use its position as a shareholder to influence policies.

Representation

36 As well as councillors, the Pension Fund Sub Committee includes representatives of a large employer (the College of North West London) and of employees (the GMBU) as non-voting, but participating, observers.

Communication

37 Considerable progress has been made in communicating with employers and employees. Developments include:-

a) a web site
b) annual benefit statements to active members and deferred pensioners
c) regular newsletters for active members and pensioners
d) regular employer updates on fund developments and scheme changes
e) A Funding Strategy Statement, setting out how the Fund plans to meet future liabilities.
f) Annual reports to both employers and employees
g) A biennial employee forum
h) Seminars to explain the scheme and proposed changes, including Induction courses and Pre-Retirement seminars.

38 It is also considered to be important that stakeholders are aware of the service standards set for responses by both Brent Council and the London Pension Fund Authority, the council's administration provider. The following service standards should be expected:-

Type of work	**Maximum Turnaround Time (working days)**
Letters answered or acknowledged	5
Estimates of benefits	5
Notifications to new pensioners	10

Transfer value quotations	20
Preserved benefits – calculate and notify	10
New starters – membership confirmation	10

Treasury Policy

39 The Pension Fund maintains cash balances both to pay for benefits and to meet private equity and infrastructure cash calls. The treasury policy will be to deposit cash balances with the council's banker, the Royal Bank of Scotland, at an appropriate rate.

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