



Brent Pension Fund Sub-Committee

Tuesday, 29 November 2011 at 6.30 pm
Committee Room 4, Brent Town Hall, Forty Lane,
Wembley, HA9 9HD

Membership:

Members

Councillors:

S Choudhary (Chair)
Mrs Bacchus
Crane
Mitchell Murray
Brown
Hashmi
BM Patel

first alternates

Councillors:

Denselow
Oladapo
Harrison
Hirani
CJ Patel
CJ Patel
HB Patel

second alternates

Councillors:

Gladbaum
Daly
Hector
Hossain

Baker

Non Voting Co-opted Members

George Fraser
Ashok Patel

GMBU
College of North
West London

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

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 part of this meeting.

The meeting will be preceded by a training session for members at 5.30 pm on emerging market equity investment, led by Dimensional Fund advisers.

Agenda

Introductions, if appropriate.

Apologies for absence and clarification of alternate members

Item	Page
1 Declarations of personal and prejudicial interests	
Members are invited to declare at this stage of the meeting, any relevant financial or other interest in the items on this agenda.	
2 Minutes of the previous meeting	1 - 6
3 Matters arising	
4 Deputations (if any)	
5 Report from Dimensional Fund Advisers (the emerging market fund managers)	
Chris Morgan and Aktar Ali, representatives from Dimensional Fund Advisers will attend the meeting for this item.	
6 Report from Henderson Global Investors	
Kevin Adams representative from Henderson Global Investors will attend the meeting for this item.	
7 Monitoring report on Fund Activity for the quarter ended 30 September 2011	7 - 26
This report provides a summary of fund activity during the quarter ended 30 th September 2011. The report also examines the actions taken, the economic and market background, investment performance and provides comments on events in the quarter.	

I have circulated reports from Henderson Global Investors and Legal & General Investment Managers.

Ward affected: All Wards **Contact Officer:** Martin Spriggs,
Exchequer and Investment
Tel: 020 8937 1472
martin.spriggs@brent.gov.uk

8 **Review of the Local Government Pension Scheme**

27 - 30

In June 2010 Lord Hutton was commissioned to chair an independent review of public sector pensions. The Commission has provided the government with interim and final reports detailing its proposals. The interim report recommended that if the Government wished to make savings to reduce rising cost pressures, raising employee contribution rates would be the most effective way to achieve that objective. This report summarises the proposals and how officers intend to respond.

Ward affected: All Wards **Contact Officer:** Martin Spriggs,
Exchequer and Investment
Tel: 020 8937 1472
martin.spriggs@brent.gov.uk

Exclusion of press and public

The following reports are excluded from the press and public as they contain a category of exempt information as specified in paragraph 12A of the Local Government (Access to Information) Act 1972, namely:

- "3. Information relating to the financial or business affairs of particular persons (including the authority holding that information)".

9 **Review of the Actuary for the Brent Fund**

31 - 34

This report details the appointment of an actuary to the Brent Pension Fund.

Ward affected: All Wards **Contact Officer:** Martin Spriggs,
Exchequer and Investment
Tel: 020 8937 1472
martin.spriggs@brent.gov.uk

This report discusses proposals to amend the asset allocation for the Brent Fund,

Ward affected: All Wards

Contact Officer: Martin Spriggs,
Exchequer and Investment

Tel: 020 8937 1472

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- The meeting room is accessible by lift and seats will be provided for members of the public.
- Toilets are available on the second floor.
- Catering facilities can be found 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, 27 September 2011 at 6.30 pm

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

Apologies were received from: Councillor Crane.

Also present – Valentine Furniss (Independent Adviser)

1. **Declarations of personal and prejudicial interests**

None declared.

2. **Minutes of the previous meeting held on 28 June 2011**

RESOLVED:-

that the minutes of the previous meeting held on 28 June 2011 be approved as an accurate record of the meeting.

3. **Matters arising**

None.

4. **Deputations (if any)**

None.

5. **Report from the performance measurement company, WM - Lynn Coventry (LC)**

LC attended the meeting for this item. In presenting her report, she outlined the overall market environment and pointed out that Local Authorities had seen positive returns on equities in the year 2010/11 although the market remained volatile. Property remained the best performing asset class over a longer term of 20 years.

In drawing attention to performance relative to the benchmark, LC informed the Sub-Committee that the Fund had achieved a positive return of 6.7% during the latest year. This compared with the benchmark return of 6.9% and the Local Authority average of 8.2%. She added however that Brent's ranking was in the 84th percentile. Over the medium and longer term, the Fund was well below the benchmark and the Local Authority average.

Members noted that over the 20 year period, the Fund achieved a return of 6.9% p.a. which compared with the UK Retail Price Index (RPI) of 2.9% p.a., representing a real rate of return of 3.9% p.a. She highlighted the attribution of the respective asset classes to the total fund performance both in the medium and longer term together with each manager's performance.

RESOLVED:-

that the report by WM measurement company be noted.

6. **Report from Fauchier Partners**

Alex Dolbey and Christopher Fawcett, representatives from Fauchier Partners, hedge fund portfolio managers, attended the meeting for this item. Alex Dolbey informed the Sub-Committee that the results for the year ending 31 August 2011 had been disappointing with negative returns of 3%. He outlined the following main actions that had been taken to address the situation:

- Removed overly conservative managers who took insufficient risk.
- Appointed additional specialist credit managers to increase exposure.
- Increased exposure to process driven managers.
- Positioned the portfolio to benefit if macro issues should re-assert themselves.

The results of the changes were initially encouraging with the Fund returning 3.9% in the second half of 2010. However, the first half of 2011 had again been very disappointing for the fund and global markets in general.

Christopher Fawcett provided further clarifications on the results and the market outlook. He informed members that the opportunity for value creation would be enhanced in the light of increases in distressed debt, bank disposals and debt restructuring. He was confident that corporate activity would present attractive opportunities in view of market volatility and high corporate cash balances.

RESOLVED:-

that the report by Fauchier Partners be noted.

7. **2010/11 Pension Fund Accounts**

The Sub-Committee received a report which introduced the final Pension Fund accounts for 2010/11. Gary McLeod (GM), a representative of the District Auditor, attended the meeting for this item.

In providing a summary of the findings he stated that subject to the completion of the final review and audit closure, the audit of the accounts was substantially complete. GM informed the Sub-Committee that the District Auditor proposed to give an unqualified audit opinion on the financial statements but would not issue her opinion until the audit of the Council's main financial statements had been completed. He continued that the draft financial statements which were

substantially complete and supported by good working papers, were submitted by the due date, and that the migration of balances to the new Oracle system was well controlled. Members noted that the financial statements submitted for audit were free from material error, missing and incomplete disclosures had been adjusted by officers and that overall, no significant weaknesses had been identified in the pension fund internal controls. There were no material differences to the pension fund financial statements on the transition to International Financial Reporting System and the pension fund financial statements had been properly compiled.

RESOLVED:-

that the report on 2010/11 Pension Accounts be noted.

8. Monitoring report on fund activity for the quarter ended 30 June 2011

The Sub-Committee considered a report that provided a summary of fund activity during the quarter ended 30 June 2011 and examined the actions taken, the economic and market background together with the investment performance in the quarter.

In summarising the main points Martin Spriggs (MS), Head of Exchequer and Investment, informed Members that the Fund had risen in value from £486m to £494m and had outperformed its benchmark over the quarter (+0.8%). This was mainly as a result of stock selection (outperformance in bonds, UK equities, Global tactical Asset Allocation (GTAA) and private equity) offset by underperformance in hedge funds. Over one year, the Fund had outperformed its benchmark (+3.3%) but had underperformed the average fund (-1.1%) as a result of lower exposure to equities / higher exposure to alternative assets and poor performance in global equities, and hedge funds.

MS outlined the main investment changes to the Brent Fund that had occurred as a result of market movements. He added that there had been a large number of retirements / early retirements during the quarter, resulting in lump sum payments from the Fund. MS referred to the problems experienced by Fauchier and measures they had taken to address them, and advised that the manager should be given time to improve (to the end of 2011 at least), but subject to close monitoring of their performance. However, the strategic question of how much should be allocated to hedge funds would be reconsidered as part of the asset allocation review.

Valentine Furniss (VF), Independent Adviser explained that the marked deterioration in investor confidence triggered by the problems in the US and the Eurozone couple with fear of below forecast world trade and inflation had affected the concluding opinion on equity markets in the investment report for the quarter ended 30 June 2011. In reference to the addendum attached to his report, VF informed members that the principal causes of the recent falls in the global markets were a lack of essential decisions to rectify fiscal deficits, weakening economic growth coupled with increasing inflation. In the light of the state of the markets, he advised a more cautious investment stance as equity markets were likely to remain flat for 2011 as a whole.

RESOLVED:-

that the monitoring report on fund activity for the quarter ended 30 June 2011 be noted.

9. **Asset Allocation Review 2011**

Members received a report that reviewed the asset allocation for the Fund, examined consultancy advice and set out a process for considering the revision of the asset allocation.

Clive Heaphy, Director of Finance and Corporate Services in his introduction emphasised the importance of the review of the asset allocation in the light of poor investment performance relative to other local authorities and the recent Actuarial Valuation. He added that the 2010 valuation of the fund indicated that liabilities were only 61% funded, which was the second worst local authority outcome out of 89 funds nationally. As a result, employer contributions for Brent were being increased from 22.9% in 2010 to 27.4% by 2013, with further increases predicted.

Staff numbers in Brent had been reduced by almost a quarter to around 2,800 as a result of severe reductions in government funding resulting in far less employee contributions into the fund in future. It was anticipated across local government that changes in pension contributions and benefits resulting from the Hutton review and other initiatives could lead to an increase in 'opt-outs' further depressing the number of future paying members. A further consideration was that the Head of Exchequer and Investment will retire in 2012. The Director advised that careful management would therefore be required to bring the fund back to a more stable position, underpinned by a long term investment strategy that would be sustainable, manageable and realistic.

MS outlined the previous changes to the asset allocation, the main reasons for under-performance of the fund against the average local authority fund and the key issues for members to consider. He continued that in order to support the asset allocation review process, the consultancy firm Mercer Ltd had been appointed to provide advice on asset allocation and to lead a training session for members. The session would also examine the main issues surrounding asset classes, risks, the deficit and the maturity of the Fund. Following the training session, officers would submit a further report recommending options for any changes to the asset allocation. He urged members to attend the meeting arranged for Monday 31 October 2011 at 2:00pm.

RESOLVED:-

that the report from the Head of Exchequer and Investment on asset allocation be noted.

10. **Investment in the clean energy and infrastructure fund**

Members gave consideration to a report that proposed a £10 million investment in the Clean Energy and Infrastructure Fund managed by Capital Dynamics.

MS set out the main aspects of the Clean Energy and Infrastructure Fund and advised members that clean energy was a very specialist area for which Capital Dynamics appeared to have relevant skills and experience. He continued that investing in the Clean Energy and Infrastructure Fund would accelerate exposure both in infrastructure and the 'green' energy theme. The investment would increase the benchmark allocation to infrastructure from 5% to 6%.

RESOLVED:-

that £10millions be invested in the Clean Energy and Infrastructure Fund managed by Capital Dynamics.

11. **Any other urgent business**

None.


12. **Date of next meeting**

The next meeting will take place on Tuesday 29 November 2011.

The meeting closed at 8.45 pm

S CHOUDHARY
Chair

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	<p style="text-align: center;">Pension Fund Sub Committee 29 November 2011</p> <p style="text-align: center;">Report from the Director of Finance and Corporate Services</p>
For Action	Wards Affected: ALL
Report Title: Monitoring report on fund activity for the quarter ended 30th September 2011	

1. SUMMARY

This report provides a summary of fund activity during the quarter ended 30th September 2011. 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 fell sharply during the quarter, but bonds were stronger as investors sought more secure assets.
- b) The Fund has fallen in value from £494m to £453m, and has underperformed its benchmark over the quarter (-1.3%) as a result of both asset allocation (overweights to equities, and underweights in bonds and property) and stock selection (underperformance in bonds, GTAA, hedge funds and emerging market equities) partly offset by outperformance in private equity.
- c) The Fund outperformed the average local authority fund return for the quarter (+1.1%), as a result of asset allocation (low exposure to equities / high exposure to alternatives, offset by relative underperformance in bonds.
- d) Over one year, the Fund has outperformed its benchmark (+0.7%). Asset allocation detracted from performance – the fund is overweight in equities / underweight in bonds against its benchmark. However, there was outperformance in stock selection (good returns from UK equities, small companies and private equity, but underperformance in overseas equities, hedge funds and bonds).
- e) Over one year, the Fund has outperformed the average local authority fund (+1.2%), mainly as a result of lower exposure to equities / higher exposure to alternative assets, but also because of good performance in UK equities and UK small caps offset by underperformance in overseas equities, bonds and hedge funds.

2. RECOMMENDATIONS

Members are asked to note this report.

3 DETAIL

ECONOMIC AND MARKET BACKGROUND - QUARTER ENDED 30TH SEPTEMBER 2011

3.1 Equity markets fell during the quarter. The UK and USA markets fell by 14%, Japanese by 11%, Germany 24%, Hong Kong by 21% and Chinese. 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, Ireland, Portugal and Spain) have affected these markets, but UK has benefited from a safe haven status. It is unlikely that rates will rise until 2013, despite inflation being above target.
- Headline inflation (RPI) rose by 5.4% in the year to October (5.2% August), and the Index of Consumer Prices (CPI) rose by 5.0% (4.5% August). It is expected that inflation may have peaked, well above the Bank of England 2% target for 2011, and should fall over a two year period as the VAT increase falls out of the figures, and spare capacity and low pay increases bear down on prices. The Bank has voted to extend the quantitative easing programme by £75b in order to increase liquidity within the banking system.
- Average earnings growth (including bonuses) was 2.2% p.a. in August (2.9% July), below the Bank of England's 'danger level' (4.5%). Unemployment (claimant numbers) has risen to 1.6m, and is likely to rise further as public expenditure is reduced, real wages fall, and taxes are raised.
- The UK economy is growing very slowly, with GDP rising by 0.5% in Q3 2011 (0.5% year on year). GDP is expected to grow by 0.5% / 1% in 2011, and by 0%-1% in 2012.
- Retail sales have risen by 0.6% in the year to September. The squeeze on incomes and the rising price of commodities is depressing demand. House prices have fallen by 1.8% over one year to October (Halifax). Mortgage approvals are only 60% of their level two years ago. Capital Economics still expects further house price falls (15%/20%).

In summary, the UK economy is growing at a very slow rate but interest rates are expected to remain low for some time. The government was using both fiscal and monetary policy to combat the downturn, but fiscal policy is being tightened over the next four years. The recovery is expected to be slow with occasional setbacks. It is increasingly possible that the UK will slip back into recession.

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 will grow by 3% in 2011 (3% 2010) following tax cuts and quantitative easing (QE) programmes, but that growth will decline to 2.7% in 2012. It is expected that Eurozone GDP will grow by 1.8% in 2011, supported by growth in Germany, but that growth rates will fall to 0.5% in 2012. The recent bail-out deal for Greece initially reduced market tension, but there are worries about future requirements for Greece and other European states. Growth in China and India is forecast to be around 9% and 8% respectively in 2011 – emerging market growth remains strong. China has raised interest rates and tightened banks' reserve requirements, while India has also raised rates. The world economy is expected to grow by between 3% and 4% 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 increased exposure to alternative assets.

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

Market (1)	Market Value 30.09.11 £M (2)	Market Value 30.09.11 % (3)	WM LA Average 30.09.11 % (4)	Fund Benchmark 30.09.11 % (5)	Market Value 30.06.11 £M (6)	Market Value 30.06.11 % (7)	WM LA Average 30.06.11 % (8)
Fixed Interest							
UK Gilts	18.5	4.1	11.6	4.5	16.1	3.3	10.7
Corp.Bonds	23.9	5.3	*	4.5	24.6	5.0	*
IL Gilts	-	-	5.0	-	1.7	0.4	4.8
Overseas	-	-	2.3	-	-	-	2.5
Emerg. Market	8.3	1.8	-	2.0	8.4	1.7	-
Infrastructure	1.2	0.3	-	-	1.2	0.2	-
Secured loans	2.3	0.5	-	2.0	4.7	1.0	0.6
Credit Opps.	9.4	2.1	-	2.5	9.3	1.9	*
Credit Alpha	12.2	2.7	-	2.5	12.6	2.5	*
Currency Fund	-	-	-	-	0.6	0.1	
Equities							
UK FTSE350	60.1	13.3	29.1	12.5	71.4	14.4	30.9
UK Small co's	14.3	3.1	*	4.0	16.2	3.3	*
O/seas - developed	103.5	22.8	33.7	22.5	121.9	24.7	34.1
O/seas – emerging	26.7	5.9	*	8.0	35.9	7.3	*
Other							
Property – UK	27.8	6.1	6.7	8.0	27.2	5.5	6.3
Property – Eu.	6.6	1.5	*	*	7.1	1.4	*
Hedge funds	39.9	8.8	1.9	10.0	41.8	8.5	1.9
Private Equity	61.4	13.6	4.1	10.0	56.0	11.3	3.2
GTAA	15.9	3.5	1.3	4.0	19.4	3.9	1.4
Infrastructure	10.4	2.3	*	2.0	9.9	2.0	*
Cash	10.5	2.3	3.7	1.0	8.1	1.6	3.7
Total	452.9	100.0	100.0	100.0	494.1	100.0	100.0

3.5 The main **investment** changes to the Brent Fund have occurred as a result of market movements, sales of UK equities and fixed interest to fund investment / payments (£4m), increased exposure to private equity (£3.8m), property (£0.3m,

being reinvestment of dividends), and infrastructure (£0.3m). There have been a number of retirements / early retirements during the quarter, resulting in additional lump sum payments from the Fund. Since the end of the quarter there has also been further investment in UK property (£0.3m), infrastructure (£5m) and private equity (£4.0).

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 30th September 2011.

Table 2: Investment Returns in Individual Markets

Investment Category	RETURNS						Benchmark/ Index Description
	Quarter Ending 30.09.11			Year Ended 30.09.11			
	Fund %	Benchmark %	WM Local Auth %	Fund %	Benchmark %	WM Local Auth %	
Equities			-14.9			-5.1	
UK FTSE350 Equities	-13.6	-13.5	-13.6	-3.2	-4.4	-4.0	FTSE 350
UK Small Caps	-11.9	-14.4		4.5	-4.5		FTSE Smallcap ex IT
Overseas - developed	-15.1	-15.1	-16.1	-12.5	-12.4	-6.2	FTSE World 75% Hedge
Overseas - emerging	-25.6	-20.1	-19.0	-	-	-	FTSE AW - All emerging
Fixed Interest							
Total Bonds	1.4	3.0	4.1	3.8	4.4	6.3	Brent benchmark
UK Bonds	8.7	8.3	3.5	8.4	7.8	4.0	FTSE UK over 15 years
Index Linked UK	-	-	6.9	-	-	12.9	-
Corp Bonds	1.9	1.6	-	2.5	2.0	-	iBoxx Sterling Non-gilt
Secured Loans	-4.6	1.0	-	3.9	3.7	-	3 month LIBOR +3%
Credit Opportunities fund	2.1	1.4	-	5.9	5.7	-	3 month LIBOR+5%
Other							
UK Property FOF	2.1	1.9	1.0	9.0	8.7	7.7	IPD Pooled index
Eu Property FOF	-5.8	1.9	-	2.8	8.0	-	IPD All properties
Hedge Funds	-4.5	1.2	-3.4	-2.7	4.7	0.5	3 month LIBID+4%
Private equity	3.7	0.1	2.1	17.0	0.5	15.1	LIBID 7 Day
Infrastructure	3.9	1.2	-	11.0	4.7	-	3 Month LIBID +4%
GTAA	-18.0	-12.9	-	-3.2	-4.4	-	FTSE 100
Cash	0.2	0.1	0.2	3.0	0.4	1.3	GPB 7 DAY LIBID
Total	-8.2	-6.9	-9.3	0	-0.7	-1.2	

3.7 Table 3 illustrates returns over three months, one year and three years. Returns for the quarter underperformed the benchmark by 1.3%, following underperformance in bonds, emerging market equities, GTAA, European property and hedge funds, and the negative impact of overweighting equities against bonds. The main stock selection factors were:-

- Fixed interest. Although government bonds gave positive returns, other markets lost as the market turned very risk averse. Both the core and satellite portfolios underperformed the benchmark. The core underperformed mainly as a result of the overweight to corporate bonds. The satellite portfolio underperformed as secured loans, credit instruments and emerging market debt investments lost value. Henderson are cautious about markets, keeping around 10% of the portfolio in money market funds.
- GTAA. Although the bond / bond and currency strategies added value, the main losses occurred as global bonds outperformed stocks. In a period of

market turmoil, the manager has reduced the risk allocation to the stock / bond strategy. This change has generated outperformance in October.

- c) Emerging market equities. The Dimensional fund fell sharply as emerging markets suffered in the market turmoil. Most of the underperformance occurred as the manager overweighted value and smaller stocks.
 - d) Property. In the UK, there have been new entrants to the Fund, allowing the manager to purchase assets at a discount. The UK property market is performing better than expected as overseas investors see UK as a sound market and UK investors look for income yields. Outperformance has arisen as a result of above average exposure to the City and West End of London Property markets, leisure and student housing. In European property, the investment in Portugal is struggling, and the manager is reducing exposure.
 - e) Hedge funds. The Jubilee Fund managed by Fauchier Partners lost value as equity and event driven strategies were affected by market falls..
- 3.8 Over one year, the Fund outperformed the benchmark (0.7%). Asset allocation detracted from performance (-0.4%) as a result of the overweight to equities / underweight to bonds. Stock selection added value (1.1%) as a result of outperformance in UK equities, UK Small Cap, and private equity outperformed the benchmark, while hedge funds, bonds and overseas equities underperformed.
- 3.9 The Brent fund outperformed the WM Local Authority average for the quarter as favourable asset allocation (underweight equities / overweight alternatives) offset relative underperformance in bonds.
- 3.10 The Brent fund has outperformed the average local authority fund by 1.2% over one year, mainly because it has had a lower exposure to equities (higher exposure to alternatives – mainly hedge funds and private equity). However, there has been outperformance in UK equities and UK small caps, partially offset by underperformance in overseas equities (the currency hedge), bonds and hedge funds.

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

- 3.11 The main activity during the quarter has been to sell stock to fund other investments and the payment of benefits, as well as further action to rebalance the portfolio so that tracking error was reduced. This has involved buying and selling FTSE 250 stocks. There have also been some purchases and sales during this quarter to invest dividends (£0.9m), improve tracking error, pay retirement lump sums, 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.
- 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 July included buying and selling stocks to improve tracking error, to invest dividends and to fund lump sums.

NEW DEVELOPMENTS AND FUTURE INVESTMENT OUTLOOK FOR THE BRENT FUND

- 3.13 Markets rose sharply in October on confidence that eurozone issues will be resolved, before falling back at the end of the month and into November on renewed Greek and southern European anxieties.
- 3.14 The infrastructure fund, managed by Alinda, has purchased the Houston Fuel Oil Terminal Company. The company owns and operates a 13.8m barrel oil storage facility, with pipeline links to major refineries and a strategic location on the widest and deepest section of the Houston Ship Canal. It is believed that the company has a strong monopoly position with good growth prospects. The Brent Fund has paid over £5m in October to Alinda to support the purchase.

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 2011 quarter report
Legal & General – September 2011 quarter report
Fauchier Partners – September 2011 quarter report
Persons wishing to discuss the above should contact the Exchequer and Investment Section, Finance and Corporate Services , 020 8937 1472/1473 at Brent Town Hall.

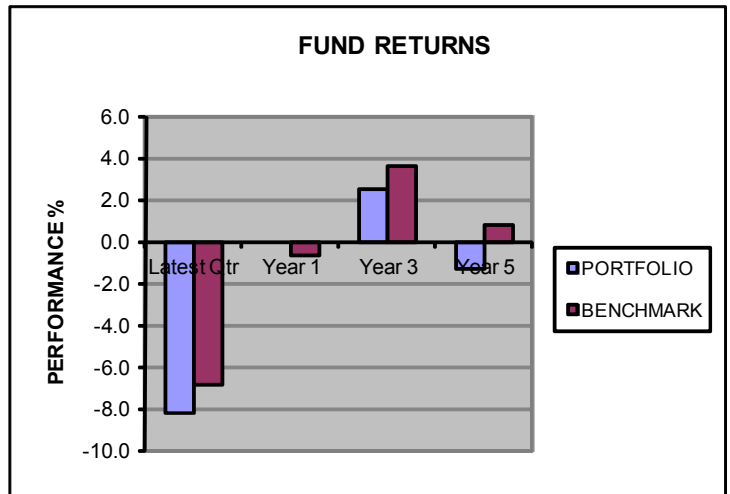
CLIVE HEAPHY
Director of Finance & CS

MARTIN SPRIGGS
Head of Exchequer and Investment

TABLE 3: PERFORMANCE FOR INDIVIDUAL PORTFOLIOS 30th SEPTEMBER 2011

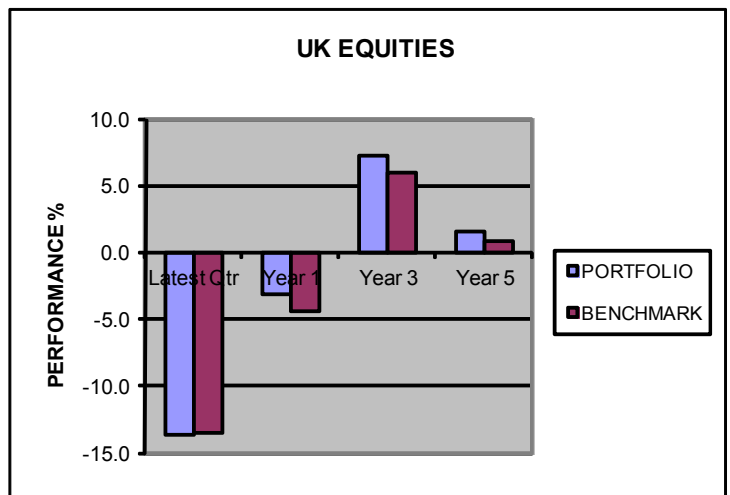
FUND RETURNS

	PORTFOLIO	BENCHMARK
Latest Qtr	-8.2	-6.9
Year 1	0.0	-0.7
Year 3	2.5	3.6
Year 5	-1.3	0.8



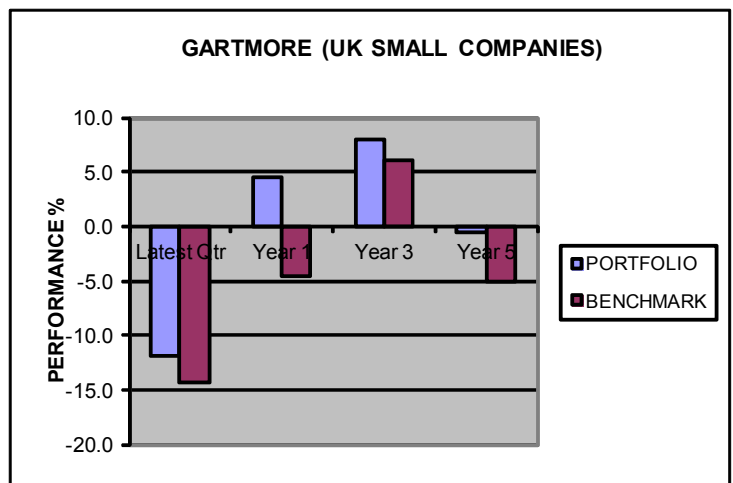
UK EQUITIES

	PORTFOLIO	BENCHMARK
Latest Qtr	-13.6	-13.5
Year 1	-3.2	-4.4
Year 3	7.2	6.0
Year 5	1.5	0.9



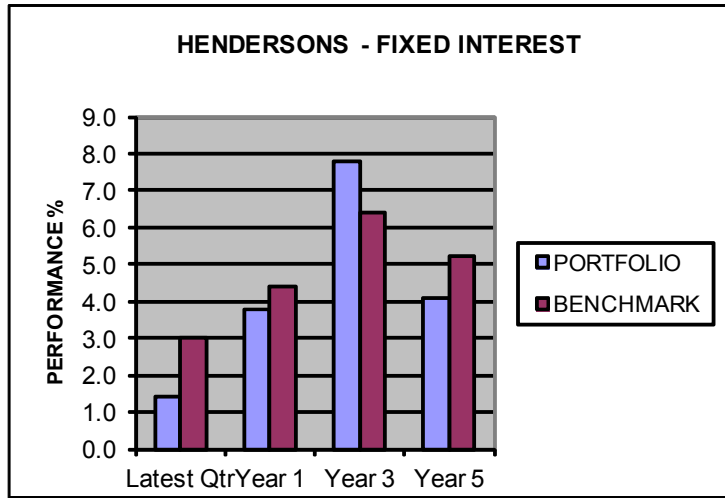
GARTMORE (UK SMALL COMPANIES)

	PORTFOLIO	BENCHMARK
Latest Qtr	-11.9	-14.4
Year 1	4.5	-4.5
Year 3	8.0	6.0
Year 5	-0.5	-5.1



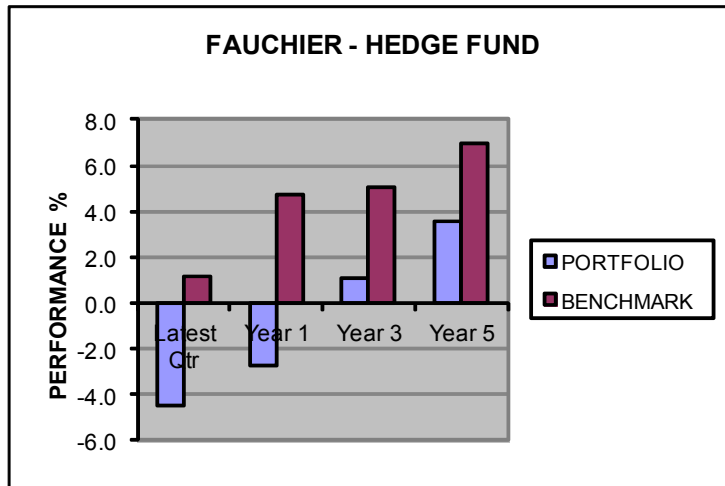
HENDERSONS - FIXED INTEREST

	PORTFOLIO	BENCHMARK
Latest Qtr	1.4	3.0
Year 1	3.8	4.4
Year 3	7.8	6.4
Year 5	4.1	5.2



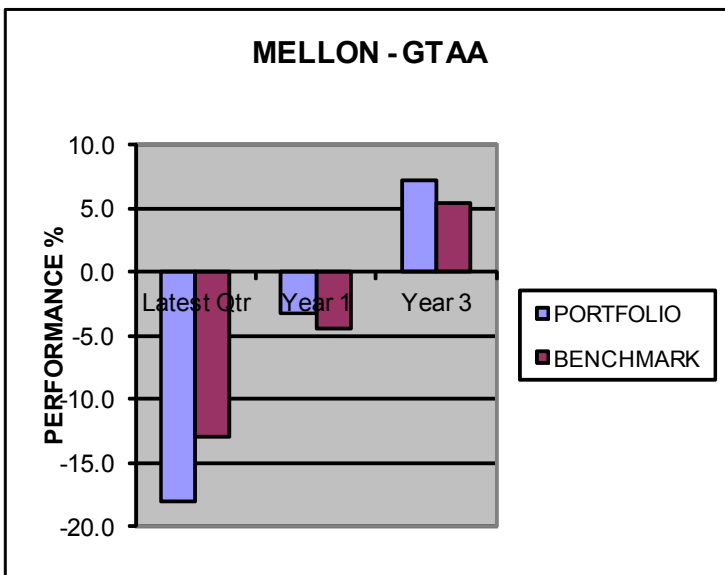
FAUCHIER - HEDGE FUND

	PORTFOLIO	BENCHMARK
Latest Qtr	-4.5	1.2
Year 1	-2.7	4.7
Year 3	1.1	5.1
Year 5	3.6	7.0



MELLON - GTAA

	PORTFOLIO	BENCHMARK
Latest Qtr	-18.0	-12.9
Year 1	-3.3	-4.4
Year 3	7.2	5.4



Report from the Independent Adviser

Investment Report for the Quarter ended 30th September 2011

Market Commentary

During the quarter it seemed that not a day went by without an emotive announcement or event which served to add further turbulence and consternation within stock markets both in the UK and across the World. This was particularly the case in the Eurozone where the indebted peripheral member countries, particularly Greece, continued to struggle with the poor state of their economies. During the quarter there were a plethora of high level meetings and summits regarding the necessary remedial measures so essential in resolving the problems.

In the UK, the coalition government's prime commitment has been to manage the measures of its austerity programme and to convince consumers and corporations alike that it is in the country's best interests, despite the current belt tightening as the medicine begins to bite with a vengeance. So far the government's programme appears to be working surprisingly well with most accepting this tough medicine. There have been relatively few strikes, although there were episodes of rioting and looting in London and other principal cities. The machinations of the UK stock market have been truly manic with daily moves of 5% or more being commonplace. Indeed, certain banks fell by 10% in a day. Between the 7th and the 19th July the FTSE 100 index collapsed by 17%.

In the USA, President Obama has had to contend with a virtual political stalemate as the Democratic and Republican parties were unable, until the very last moment of the set deadline, to compromise on resolving the fiscal budget deficit issues. Had they not done so the White House administration and those of the individual states would have been at a virtual standstill and in default. At the Federal Reserve Board, Ben Bernanke has made a number of gloomy statements about the economy and has continued to drop hints that the only real way forward is to introduce another bout of quantitative easing. The downgrade of Treasury Stocks by the rating agency Standard & Poors was also a severe blow to the international standing of the USA in its capacity as the world's largest economy.

In Japan, as is so often the case, there was little news to report of any substance other than yet another change of prime minister, the sixth in 5 years. Yoshihiko Noda of the leading Democratic Party replaced Naoto Kan whose government had presided over a period of inept leadership. There are signs that Japan continues to recover at a faster pace than expected from the devastations of the tsunami and earthquake.

In the Asia/Pacific region, the Chinese government has demonstrated skill at managing strong economic growth whilst curbing inflation. It has been helped by the People's Bank of China who has generally been successful in controlling the strength of its currency the renminbi. China continues to relish its increasing role on the international scene as its economy becomes ever more powerful. This economic strength has also benefitted the export trade of other Asian countries, so great is demand from China. Further a field China appears to have an insatiable demand for minerals and also products with which to build its infrastructure requirements, vide highways and airports. It is interesting to note that approximately 64% of the world's more affluent middle classes live in Asia. That said, poverty levels, particularly in China, remain high.

The index returns and currency movements for the quarter ended 30th September 2011 are shown in the tables below:-

Index returns expressed in sterling

	Indices	Q/e 30.09.11
		%
Equities		
Japan	FTSE Developed Japan	-3.1
North America	FTSE North America	-11.8
UK	FTSE All Share	-13.5
Asia/Pacific	FTSE Developed Asia Pacific (ex Japan)	-18.8
Emerging Markets	MSCI Emerging Markets Free	-20.1
Europe	FTSE Developed Europe (ex UK)	-24.2
Fixed Interest		
UK Gilts	FTSE British Government All Stocks	8.3
UK ILGs	FTSE British Gov. Index Linked Over 5 years	7.8
Corporate Bonds	Merrill Lynch Sterling – Non Gilts All Stocks	1.6
Property	IPD	1.2*
Cash	Merrill Lynch LIBOR 3 Month	0.2

* The IPD UK Property return from 30th June 2011 to 31st August 2011 (the returns for September are not yet available)

Currency Movements for quarter ended 30th September 2011

Currency	30th June 2011	30th September 2011	Change %
USD/GBP	1.605	1.558	-3.0
EUR/GBP	1.107	1.161	4.9
USD/EUR	1.450	1.342	-7.5
YEN/USD	80.760	77.080	-4.6

As a result of the adverse factors described in the preceding paragraphs together with the state of confusion and fear, it is scarcely surprising that equity returns shown in the above table are poor with the exception of Japan (-3.1%) having the least negative return. This, no doubt, reflects the fact that the degree of debt within that country is considerably less than elsewhere. Next in line came the USA (-11.8%). In view of its troubled politics and economy it could have been expected to decline to a greater extent. Part the reason is that corporate results were considerably better than expected and that, as experienced in past periods of economic weakness, the USA is usually one of the first global economies to recover. The UK (-13.5%) was less awful than other returns due to the recognition that its coalition government's austerity measures are seen to have a reasonable chance of ultimate success in turning the ailing economy around. The Asia/Pacific return (-18.8%) reflected apprehension that the strong rates of GDP growth would slow due to a drop off in world trade and that the Chinese economy might even experience a hard landing. Additionally, past experience shows that when there is a crisis of investor confidence, Asia/Pacific markets suffer more than most as global investors de-risk their portfolios and repatriate funds. Essentially the same applies to Emerging Markets (-20.1%) despite the relative strength of many of their economies. Finally, it is understandable that Europe was backmarker in registering a negative 24.2% return. The severity of this poor performance is simply reflecting the much discussed acute problems within the Eurozone and the worry that a successful solution may not be found in the near future with the difficulties of gaining the agreement of all the institutions and governments involved who, up to the quarter end,

had not demonstrated, with sufficient urgency, the necessary leadership unanimity to enact the essential decisions.

Against the above litany of woe the returns from the “Fixed Interest” subsector provided some much needed succour to investors in recording universally positive results as a refuge was sought from other asset classes perceived to be high risk. It is interesting to note that 10 year gilt yields dropped to 2.24%, the lowest since 1899 according to the Bank of England. By comparison, the yield on US 10 year Treasury bonds fell to 1.97%, the lowest recorded since 1950. This clearly shows the length to which investors were prepared to go in order to achieve so called sanctuary. At the head of the leader board were UK Gilts (+8.3%) as investors sort the safe haven of sovereign debt. Next came UK index linked gilts (+7.8%) on the assumption that inflation might continue to rise, especially if the Bank of England has to resort to a further quantitative easing programme which appears increasingly likely. Corporate bonds managed a positive 1.6% return, largely due to further demand based on the still attractive yields they provide; often in excess of equities. In sum, the Fixed Interest sector yet again proved its worth in times of acute turmoil. A form of portfolio insurance you might say. In any fixed interest portfolio, apart from the traditional subsectors of government debt, it still appears appropriate to include an enhanced subsector to include hedge type transactions, swaps and derivatives. It is an amalgam of these two subsectors that should in the longer term outperform a wholly traditional portfolio.

The property returns for the quarter are not yet available. Suffice it to say that over the months of July and August the return was a still positive 1.2%. Against the prevailing adverse conditions, this should be seen as a resilient performance.

UK

Positive Influences

- The Bank of England claimed success in relation to its £200B quantitative easing programme in 2009/10 and suggested that it had “economically significant effects”.
- The purchasing managers’ index for September rose to 51.1 from 49.4 in August; a better result than expected.
- The Treasury has started talks with pension funds to explore the possibility of them investing in the nation’s infrastructure. This is already the practice in North America.
- On 8th September the Bank of England left interest rates on hold at 0.5%.
- The Office for National Statistics reported a miniscule 0.1 rise in August’s manufacturing output. The annual increase was 1.9%.
- The National Institute for Economic and Social Research estimated that the economy grew by only 0.2% in the quarter to 31st August.
- There has been clear evidence of directors buying shares in their own companies. Also share buy-back programmes have increased.

Negative Influences

- CPI inflation increased to 4.5% in July from 4.4% in June.
- The banks will face a bill totalling £6B as a result of Sir John Vickers independent commission on banking. He suggested structural changes in order to ring fence retail banking and also that the banks should provide greater detail on charges.

He maintained that banks should separate their trading and investment banking activities. The principal aim is to make banks better capitalised with less leverage. Both George Osborne, Chancellor of the Exchequer and Vince Cable, the Secretary for Business have endorsed the report.

- The Office for National Savings reported that, in the second quarter of 2011, GDP rose a meagre 0.1% compared with estimates of 0.2%.
- The Institute of Supply Management's September survey showed its non manufacturing activity index receded to 53.0 from August's 53.3.
- A rumour started that the Royal Bank of Scotland might still need a further injection of capital to further boost its core tier one capital ratio (a measure of financial strength).
- The Halifax House Price Index fell 1.2% in August.
- Rail fares are to rise by an inflation busting 8.0% in 2012.
- On 10th August the Bank of England reduced its estimate of GDP growth for 2011 from 1.9% to 1.7%. For 2012 it also reduced its estimate from 2.5% to 2.1%. These estimates appear to be overly optimistic.
- The National Institute for Economic and Social Research stated "subdued domestic demand will hinder any meaningful recovery this year". The Institute estimates that consumer spending will fall by 0.8% in 2011. In 2012 it estimates unemployment to increase to 8.3% with the inflation rate averaging 1.9%. This last figure seems unlikely to be achieved.
- In the 3 months to August the unemployment rate rose to 8.1%, the highest rate for 15 years.
- There is growing evidence that poor aviation links increasingly cause the UK to miss out on lucrative trade with the emerging markets and elsewhere.

USA

Positive Influences

- The Institute for Supply Management's manufacturing index rose to 51.6 in September (50.6 in August).
- The Federal Open Market Committee introduced a programme named "Twist". Its aim being to sell short dated Treasury Stock and to buy bonds of longer maturity in order to reduce long term interest rates, effectively flattening the yield curve.
- The rate of GDP growth in the second quarter of 2011 was revised up to 1.3% from 1.0%.
- The Conference Board's consumer confidence index increased marginally in September to 45.4 from 45.2 in August. By comparison the University of Michigan's confidence index increased to 57.8 in September, up from 55.7 in August.
- On 9th August, the Federal Open Market committee stated "the committee currently anticipate that economic conditions indicating low rates of resource utilisation and a subdued outlook for inflation over the medium term are likely to result in exceptionally low levels for the federal funds rate at least through 2013". It added that it was prepared to employ its policy tools "as appropriate" under enormous political pressure and the threat of economic gridlock.
- On 26th August, Ben Bernanke, head of the Federal Reserve Board, stated "the central bank is prepared to employ its tools as appropriate to

promote a strong recovery". This may or may not include an additional quantitative easing programme.

- The Republican and Democratic Parties finally agreed a series of cuts totalling \$2,100B.

Negative Influences

- Factory orders fell by 0.2% in August.
- Sales of previously owned houses fell by 3.5% in July, markedly lower than estimates of +2.7%.
- On 5th August the rating agency Standard & Poors downgraded its US sovereign credit rating from AAA to AA.
- On 16th August, the Fitch rating agency lowered its Triple A status for US sovereign debt.

Europe

Positive Influences

- José Manuel Barroso, President of the European Commission, suggested that the Commission should be given a larger role in sorting out the Eurozone's financial problems.
- Silvio Berlusconi's centre right government was able to pass the country's austerity budget.
- There is a possibility that China might buy Italian bonds. In that regard the China Investment Corporation sent a delegation to Rome.
- On 1st September, the European Central Bank left its interest rate on hold at 1.5%.
- On 6th September, the Swiss National Bank announced it would prevent its exchange rate going through SF1.20 to the Euro in order to damp down investor flights to the perceived safe haven of its currency.
- There are signs that Eurozone governments are keen to ban short selling.
- On 29th September the German government, despite its fragile coalition led by Chancellor Angela Merkel, voted in favour of adding to the European Financial Stability Facility (EFSF). This was partly in response to the urgent request by the International Monetary Fund that the EFSF should be increased from €440B to a range of €1,000 to 3,000B in order to boost the fund's credibility.

Negative Influences

- On 6th July the rating agency Moody's downgraded Portugal.
- The European Commission's economic sentiment indicator for September retreated to 95.0 from August's 98.4.
- Eurozone inflation in September rose to 3.0% p.a., a 3 year high level.
- It was announced that the Franco-Belgian bank Dexia might have to be suspended prior to a break up. So much for July's stress testing of European banks in which Dexia was placed 12th out of 91!
- In September Germany's inflation rate rose to a 3 year high at 2.8% compared with 2.5% in August.
- On 14th September, the rating agency Moody's downgraded the banks Société Générale and Credit Agricole.

- On 15th September, a UBS bank propriety trader used a Delta One derivative based on synthetic exchange traded funds and caused a loss of \$2B. Small wonder that the Vickers Commission proposes to ring fence such activities.
- Greece's second quarter GDP rate collapsed by 7.3% p.a.
- The Eurozone's purchasing managers' index for August slipped a minuscule 0.1 to 51.5.
- The Eurozone's unemployment rate registered its third consecutive rise to 15.7% (France 9.9%, Spain 21.1% and Germany unchanged at 6.1%).
- The European Commission's Economic Sentiment Index decreased to 98.3 in August (July 103.0).

Japan

Positive Influences

- On 24th August, it was announced that Japan was to contribute up to \$100B from its foreign exchange reserves to back up its overseas investments.
- On 30th August, Yoshihiko Noda, the head of the Democratic Party, became the sixth prime minister in 5 years replacing the inept Naoto Kan who had proved to be yet another weak prime minister, seemingly unable to enact the sufficiently strong legislation that the Japanese economy so badly needs to resuscitate it.

Asia/Pacific

Positive Influences

- Australian second quarter GDP grew 1.2% (first quarter -0.9%). Consensus estimates ranged from +0.9% to +1.0%.
- Global corporations are increasingly launching initial public offerings in the East at the expense of the West.

Negative Influences

- China's purchasing managers' index slipped to 57.6 in August from 59.6 in July.
- The National Bureau of Statistics reported that China's consumer inflation inched up to 6.5% in July from 6.4% in June.
- On 6th July China raised interest rates for the fifth time in 8 months. The benchmark 1 year lending rate was increased by ¼% to 6.56% and the 1 year deposit rate was lifted by 11 basic points to 3.5%.
- India's second quarter GDP growth receded to 7.7% from 8.8% a year ago.

Conclusion

In looking to the future the crystal ball is particularly opaque. However, at such a critical time in the market place investors, both institutional and private need to dispel the prevailing fog of confusion and to receive as clear as possible guide to the future as the current circumstances allow. Here it is:-

- In the UK, interest rate levels are virtually certain to remain at extremely low levels for quite some time to come. Thus, the return on cash deposits should be negligible. After the pronounced falls in equities it is quite possible to find high

quality companies standing at seemingly attractive levels with their yields well above those of cash and gilts. It therefore seems likely that nimble investors will take advantage of these attractive ratings, particularly with regard to those companies with well covered dividends, the ability to consistently grow earnings with strongly financed balance sheets. The avoidance of a double dip recession will be close run thing. More likely will be anaemic GDP growth as the economy gradually recovers, but hampered by a continuation in the rise in inflation.

- In the USA, the White House will remain in an invidious position for the remainder of President Obama's first term of office as he has effectively lost his political backing for the essential legislation that the nation so urgently needs to enact. Unemployment will be a crucial factor as will corporations' ability to improve productivity and to boost capital investment.
- In the Eurozone. As has already been mentioned, it will be vital that economic and fiscal union is agreed (to include the formation of a central budget office) and that the ECB, the IMF, the European Commission and the Group of Twenty can come together to at last agree a definitive timetable for the urgent legislation needed to guarantee the future both of the Eurozone and the Euro. The proposal for a €2,000B European Financial Stability Facility with sufficient firepower is a step in the right direction. A resolution of all the current Eurozone issues will inevitably take time, but it now appears that such a resolution will eventually be made. Of course, any agreement within the Eurozone was always going to be difficult in the light of its 17 members. As with the UK, high quality equities have sunk to attractive high yielding valuations. It should not be forgotten that 20% of international trade is accounted for within Europe.
- In Japan, much will depend on the policies enacted by the new prime minister and the ability of his government to introduce legislation much more conducive to the avoidance of a return to deflation.
- In Asia/Pacific, China will continue to be the focal point of the region. Its rate of GDP growth may ease somewhat, but should still be at an enviable rate compared with the Western Hemisphere nations and be able to avoid a hard landing. At some point it seems probable that China will manage to achieve full convertibility of its currency the renminbi which should also be held more widely within international currency reserves.

It is a prerequisite to economic progress that the respective banking systems should continue to be purged until they are fully transparent with no further well concealed skeletons lurking in cupboards. It is of paramount importance that banks should be deleveraged and be able to demonstrate that they are more fully capitalised in order to cope with all eventualities. Never again must banking systems be able to create the same havoc they have in successive episodes.

It is essential that the rating agencies be better regulated. It stands out that they should be far more pro-active with their modus operandi. Thus delivering a much improved early warning system.

So, wither the UK and global equity markets between now and the year end? Despite the risk of being a hostage to fortune, it seems reasonable to suggest that, for the reasons already given, prudent investors should take advantage of current attractive

equity valuations and that most markets should be modestly higher by the year end despite the sporadic bouts of pessimism by some commentators. This applies both to Western and Eastern hemisphere nations, but particularly to those whose markets suffered in the quarter ended 30th September 2011. If this general surmise is proved wrong it will probably be because World trade is weaker than forecast or that the economies of the UK and USA in particular should stall back into recession. Another paramount influence will be the success or otherwise of a new and better-funded Eurozone Alliance. Fixed Interest markets on the other hand seem vulnerable to the fact yields thereon are so historically low, particularly when adjusted for inflation. They also look expensive in relation to equities.

In the longer term it does seem that at their current levels Emerging Markets investments have many obvious attractions which the markets are tending to underestimate. This applies equally to equities, debt and currencies. Furthermore, to invest in emerging markets is to increase a pension fund's globalisation which appears a highly desirable theme for the medium and long term.

With regard to other asset classes, private equity investors have continued to benefit from the issue of high quality new funds both in the UK and globally together with attractive prices available in the secondary markets. On a long term basis this asset class should continue to produce strong returns when measured against equity markets. The alternative asset classes of Hedge Fund of Funds, Foreign Exchange, Commodities and Global Tactical Asset Allocation have all continued to be volatile, but that is their nature. They clearly are all capable of enhancing a pension fund's overall performance, but strong nerves are most definitely required together with a close short term performance monitoring system with which to measure the respective managers. In particular, the performance of Hedge Fund of Funds has experienced a soft patch due in the main to too much correlation within the market place. This could now change. The Foreign Exchange class has had to contend with the trade protection manoeuvring of central banks e.g. China and Switzerland. There continues to be a pronounced interest in the currencies of mineral backed economies like Australia, Brazil and Norway. Within the Commodity class a principal influence continues to be the China factor and, of course, the level of World trade.

In these most uncertain times, particularly after pronounced falls in most investment markets, investors, particularly of a nervous disposition, find it difficult to cope with the patience and mind set required to travel through the most adverse conditions and to await recovery. At such times those of a more pessimistic nature begin to wonder whether it will ever be the same again. Be assured that there have been many similar draughts in the past and markets have always recovered, admittedly after varying periods of time. This time should be no different, although it is hard to gauge how long a meaningful recovery will take.

Valentine Furniss
13th October 2011

Investment Update for the Month of October 2011

The index returns and exchange rate movements for the month of October are shown in the tables below:-

	Indices	Month ended 31.10.11
		%
Equities		
Asia/Pacific	FTSE Developed Asia Pacific (ex Japan)	11.1
Emerging Markets	MSCI Emerging Markets Free	9.3
Europe	FTSE Developed Europe (ex UK)	8.4
UK	FTSE All Share	7.9
North America	FTSE North America	7.0
Japan	FTSE Developed Japan	-3.8
Fixed Interest		
Corporate Bonds	Merrill Lynch Sterling – Non Gilts All Stocks	1.8
UK Gilts	FTSE British Government All Stocks	1.1
UK Index Linked	FTSE British Gov. Index Linked Over 5 years	-0.2
Property	IPD*	N/a
Cash	Merrill Lynch LIBOR 3 Month	0.1

* The IPD UK Property return from 31st August 2011 to 30th September 2011 was 0.6%

Currency movements for month ended 31st October 2011

Currency	30th September 2011	31st October 2011	Change %
USD/GBP	1.558	1.614	+3.6
EUR/GBP	1.161	1.157	-0.3
USD/EUR	1.342	1.395	+4.0
YEN/USD	77.080	77.975	+1.2

The tables above show what a difference a month has made, particularly within equity markets. For October all markets, with the exception of Japan, recorded worthwhile gains, demonstrating a measure of recovery from the awful returns for the quarter ended 30th September 2011. Best in class was Asia/Pacific (+11.1%) and second was Emerging Markets (+9.3%) clearly reflecting the fact that these two regions had been oversold during the quarter when their returns had been (-18.8%) and (-20.1%) respectively. This demonstrates that, in times of acute market duress and fear, investors tend to repatriate funds and reduce geographic risk by, in particular, downsizing their holdings in the Eastern Hemisphere countries, especially those deemed to be in the emerging category. On a longer term view, to reduce holdings in countries with relatively faster growing economies will surely prove to be a cause for regret. The European return at +8.4% showed a robust recovery from the quarter's negative return of (-24.2%). Next came the UK recording a substantial +7.9% as the coalition Government appeared to be coping with both the austerity programme and the fiscal deficit with more success than had originally been expected, despite the understandable fears of strikes, particularly in relation to the emotive subject of personal pensions. North America returned +7.0%, partly due to the perception that so far no obviously strong Republican candidate has emerged to challenge President Obama in next year's elections. Furthermore, there were signs that economic growth just might be recovering at a faster rate than generally forecast. Last, Japan came in with a poor return of -3.8%. Not really surprising as the new government has still to show that it is prepared to

implement those measures that the nation has needed for so long. Additionally, the country is still in the process of recovering from the devastation caused by the earthquake and tsunami.

Within the Fixed Interest arena returns were modestly higher with corporate bonds leading at +1.8% as investors were attracted by their relatively high yields (compared with cash), particularly on new corporate issues. UK gilts returned a modest 1.1%, scarcely surprising in view of the quarter's substantial return of +8.3%. It should be stressed that yields on UK gilts are now historically extremely low, reflecting the fact that gilts, particularly at the shorter end, are still seen as a sanctuary in times of great turmoil. The return on index linked gilts was a marginally negative -0.2%. Again not surprising in view of its substantial +7.8% return for the quarter. It could be that index linked gilts are now over discounting a rise in inflation.

The property return for the month was not available. However, the return for September was a modest +0.6% which compares with the cumulative positive return for June, July and August of 1.2%. In short, property is continuing to make consistent progress, but at a moderate pace. Within the constituent sub sectors of property, office property has continued to perform well. However, the retail sector has been relatively poor.

Without doubt the principle driver of markets in October continued to be the machinations within the Eurozone as it struggled to find a workable and sustainable solution, not only for the continuance of its very existence, but also for the future of the Euro currency. A plan was unveiled on the 26th October when the following stipulations were announced:-

- The firepower of the European Financial Stability Facility (EFSF) would be increased with the possible backing of the IMF and prosperous nations like China.
- The banks' tier one capital ratios to be increased to 9.0%.
- Greek bond holders would receive a 50% haircut.

Certainly the above stipulations constituted a vital step forward and served to calm stock markets and to dissipate some of the fog which had surrounded the Eurozone for so long.

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

UK

- The Bank of England announced its estimate of GDP growth for the fourth quarter of the year was "close to zero". This compares with the bank's previous estimate made in August of 0.4%. It should be stressed that the bank's record of estimating the rate of GDP growth and also inflation is extremely poor. On the 19th October the Bank of England introduced a further £75B quantitative easing programme for the purchase of gilt edged stock over the ensuing four months.
- September CPI rose to 5.2% which is close to a 20 year high. RPI increased to 5.6%. Mervyn King stated "we were on track, but the problems in the Euro area and the marked slowing in the World economy have lengthened the period over which a return to normality is likely".

- It has become increasingly difficult for home owners to access mortgages from the banks.
- The August trade deficit decreased to £1.9B from £2.3B in July. This was a better result than generally expected.
- August's industrial production rose +0.2% whilst manufacturing output receded by 0.3%.
- On 7th October, Mervyn King admitted that this "could be the worst financial crisis ever".

USA

- Third quarter GDP rose a heartening +2.5% p.a., up from +1.3% p.a. in the second quarter. This was better than expected.
- Real disposable income receded by 1.7% in the third quarter.
- The Conference Board's index of consumer confidence was 39.8 for October, markedly lower than September's 46.4.
- CPI inflation in September was 0.3%, a fraction lower than the 0.4% recorded for August.
- Retail sales in September were up 1.1% versus estimates of +0.7% and the +0.3% in August. This was partly due to an improvement in the level of car sales.
- 103,000 new jobs were created in September against a revised figure for August of +57,000. This was a much better result than expected although the unemployment rate remained stubbornly high at an unchanged 9.1%.
- On 9th October the Federal Reserve Board created "Operation Twist", a programme designed to lengthen the duration of its stimulus resources by selling \$400B short dated Treasury Stock to buy longer dated debt.

Europe

- Mario Draghi is to take over from Jean Claude Trichet as head of the ECB on 1st November. He comes with strong credentials.
- In quarter three the Spanish unemployment rate reached 21.5%.
- The Eurozone purchasing managers' index decreased to 47.2 in October from 49.1 in September.
- With regard to the French election in May, Francois Hollande is emerging as a strong challenger to Sarkozy. He represents the "Gauche Molle" (the soft left).
- On 14th October Berlusconi's coalition government narrowly survived a confidence vote. There could well be an Italian general election much sooner than the due date in early 2013.
- The rating agency, Moody's, downgraded Italy's credit status. This was no surprise at all.

Asia/Pacific

- On 27th October, Li Daokui, a member of China's central bank monetary policy committee, said "it is in China's long term and intrinsic interest to help Europe because they are one of our biggest trading partners".
- President Hu Jintao and premier Wen Jiabao are to step down in approximately a year's time after a decade in office.
- China's third quarter GDP grew by 9.1%. This was less than expected.

- China's September exports rose at a rate of 17.0% p.a. (August +25.0%p.a.) whilst imports increased by 21.0% p.a. (August +30.2%p.a.).
- China's CPI for August was 6.2% against the 6.5% recorded for July.
- On 25th October the Reserve Bank of India raised interest rates by ¼% to 8 ½% ostensibly to combat inflation.

So what has happened in the month of October to affect the main conclusions reached in the investment report for the quarter ended 30th September 2011? The recent plan of action and essential initiatives to solve the problems besetting the Eurozone has been pushed further out following the unexpected announcement on 31st October by George Papandreou, the Greek prime minister, to hold a public referendum on whether they would be prepared to accept the harsh remedial measures announced on 27th October to rescue their economy. Markets hate waiting and this will surely be negatively reflected as most stock markets, especially within Europe, establish a new level. But even when markets do eventually settle down, what then? Much will obviously depend on the success or otherwise of the measures announced on 27th October. If indeed they can be seen to be implemented in full over a reasonable period of time and if the measures are not merely a short term cobbled together patching exercise. Then markets should at last make some meaningful progress and reflect the improved conditions for Eurozone capitalism.


6th November 2011

Addendum

No sooner had the investment brief for October 2011 been completed then it became necessary to add an addendum with regard to the events in Greece. The position is that the European Union had agreed some essential measures to finally tackle the Greek financial problem. This was welcomed by markets as it was felt that the measures had a reasonable chance of succeeding, albeit over a long period of time. Next came the totally unpredicted announcement by George Papandreou that he was to hold a public referendum with regard to the acceptability of the stringent European Union bail out measures. This stunning volte face and piece of political pantomime coincided with the summit meeting of the Group of 20 and, indeed, high jacked its agenda. At this meeting Angela Merkel and Nicolas Sarkozy in particular made it abundantly clear to Papandreou that if he continued with the proposed referendum then the next imminent tranche of rescue funds would be withheld. Thus effectively bankrupting Greece. Papandreou, under intense international pressure, then cancelled the intended referendum programme. The result of all this is that international confusion and acute stock market anxiety has returned with a vengeance. At the time of writing it is quite impossible to forecast what the outcome will be.

When it comes down to the wire, Greece is clearly bankrupt. Can the Eurozone afford to keep the country as a member? Probably not. In which case a way will have to be found for the least damaging exit. The time has surely come to bite the bullet and for Greece to stop holding to ransom not only its much larger Eurozone peers, but also other involved global economies. It may very well be that the Eurozone will now have to legislate the exit strategy for any failed state. This will take time. Meanwhile stock markets will continue to worry about contagion and its effect on other weak economies, like Italy.

Valentine Furniss

	<p style="text-align: center;">Pension Fund Sub Committee 29 November 2011</p> <p style="text-align: center;">Report from the Director of Finance and Corporate Services</p>
<p>For Information</p>	
<p>Local Government Pension Scheme – Savings Proposals</p>	

1.0 Summary

In June 2010 Lord Hutton was commissioned to chair an independent review of public sector pensions. The Commission has provided the government with interim and final reports detailing its proposals. The interim report recommended that if the Government wished to make savings to reduce rising cost pressures, raising employee contribution rates would be the most effective way to achieve that objective. As the Local Government Pension Scheme (LGPS) is the only funded public sector scheme the government have agreed that the LGPS may find alternative ways of making the required £900 million savings before April 2015, the proposed date for changes to all public sector schemes. On 7th October the government issued a consultation paper to administering authorities detailing approaches to achieving the required savings. This report summarises the proposals and how officers intend to respond.

2.0 Recommendations

2.1 That members note the report and that a further report will be made detailing the proposed changes to the LGPS when the outcome of current negotiations is known.

3.0 Detail

3.1 In 2008 a revised LGPS scheme was introduced with the objective of reducing the cost pressures on the scheme. However, the 2010 Actuarial Valuation has shown that increased costs arising from longevity and poor returns need to be further addressed. The government has already reduced long term costs by changing the inflation measure from the Retail Price Index to the Consumer Price Index, but it is felt that further changes are needed to mitigate employer contribution rates.

3.2 The consultation paper issued by the Department for Communities and Local Government (DCLG) proposes that the LGPS may make cost savings via a combination of member contribution increases and reduction in accrual rates (the percentage of salary earned as pension each year). There are two proposals for achieving the measures which in total represent an average percentage increase of 3.2% in member contributions.

3.3 The Local Government Group (LGG) have previously given advice to the DCLG, and their suggestions have been distributed to administering authorities. Their proposals are designed to provide more fairness and choice to members. A summary of these have been added to those of the DCLG below.

DCLG Proposals

3.4 In order that the cost saving measures achieve the commission's aim of fairness to members the DCLG has set the following parameters which protect the lower paid:

- there should be no increase in employee contributions for those earning less than £15,000
- there should be no more than a 1.5 percentage point increase in total by 2014-15 for those earning up to £21,000. This amounts to a 0.6 percentage point increase in 2012-13 on a pro-rata basis
- high earners will pay more, but no more than 6 percentage points (before tax relief) by 2014-15. This amounts to a 2.4 percentage point cap in 2012-13 on a pro-rata basis

3.5 DCLG Option 1:

- Increase member contributions = £450m scheme saving
- Decreased member accrual rate = £450m scheme saving

A phased increase in employee contributions is proposed starting in 2012/13, along with a change in the current pension accrual rate of 1/60th of final pay for each year of service. This would reduce to 1/64th for service between 1 April 2013 and 31 March 2014, and to 1/65th for each year of service after 31 March 2014.

3.6 DCLG Option 2:

- Lower increase to member contributions than Option 1= £300m scheme saving
- Decreased member accrual rate greater than Option 1= £600m scheme saving

As shown the savings from member contributions would be at a lower level than in option 1 but offset by greater reductions in the rate at which future pensions accrue. The Government suggest that one approach could be an increase of employee contribution rates from April 2012 to raise £300m plus a change in the scheme accrual rate to raise the remaining £600m. Under this option the accrual rate would reduce to 1/67th per year of service built up after March 2014.

3.6 LGG Options 1, 2 and 3 – Note that these are the Local Government Group’s response to previous consultations with the DCLG.

- Change the normal retirement age, for future service accrual, to 66 from 01.04.14
- no increase in employee contributions for staff with full-time equivalent earnings of less than £15,000, a moderate increase for those earning between £15,000 and £21,000 of 1.5 per cent and an increase of between 2 per cent and 2.5 per cent for those earning over £21,000
- choice for employees, by giving those with earnings of £15,000 or more the option of taking a reduced pension accrual rate instead for future service from April 2014. Any employees with earnings of less than £15,000 would have the option of taking a reduction in their contribution rate but would, as a result, have a reduced pension accrual rate for future service from April 2014

Comment

- 3.7 There is a pressing need to improve the funding level of schemes and reduce future liabilities falling on employers. The proposals target the headline need to address those costs but do not fully consider other implications and potential consequences. Local authorities have made proposals to mitigate some of the damaging consequences, such as staff opting out and the confusion and administrative difficulty involved in frequent changes to the scheme. It should also be noted that the teachers’ pension scheme is also part of the review.
- 3.8 All of the above proposals introduce a further layer of complication to the scheme. Members will be aware that the LGPS accrual rate was amended in 2008. This rate will change again in 2015. Other amendments are also proposed, such as that benefits would be based on career average earnings. Repeated changes will be difficult to communicate to members and do not represent the simplicity aimed for by the commission. Confusion, mistrust and steep increases in contribution rates may result in significant numbers of staff opting out of the scheme. If this trend were to persist there may be a need for councils to inject cash into the fund in addition to the current employer contributions, and an important recruitment tool may be lost. The reality remains that measures must be taken but that there must be a trade off between cost saving and simplicity.
- 3.9 There currently exists inequality between the various public sector pension schemes. For example members of the Civil Service “Classic” Pension Scheme currently pay a 1.5% contribution rate. The accrual rate of the scheme is 1/64 (when taking into consideration the pension and guaranteed lump sum) A 3.2% increase in top civil servants pension contributions would result in a total contribution of 4.7%. This compares to the LGPS, where a social worker earning £21,001.00 currently contributes 6.5% of pay – they would be required to pay incrementally up to 8.3% under option 1 or up to 7.5% under option 2. The social worker would accrue benefits at a similar rate to that of the Civil Servant. This is inequitable and does not address the goal of fairness across public sector pension schemes.
- 3.10 Officers intend to respond to the consultation requesting a simpler and fairer approach. It will be argued that the most sensible proposal would be to reduce the accrual rate, thus reflecting that staff will work longer, but temper proposals to

increase contributions at a time when pay increases are at a minimum. It will also be sensible to introduce benefit changes at one point in time so that administration is simplified.

4.1 Financial Implications

4.2 These are covered in the detail of this report.

5.0 Legal Implications

5.1 There are no legal implications arising from this report

6.0 Diversity Implications

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

7.0 Staffing/Accommodation Implications

7.1 These are covered in the report

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