

Item No.	Classification: Open	Date: 2/12/2003	MEETING NAME EXECUTIVE
Report title:		POSITION STATEMENT ON THE SOUTHWARK COUNCIL PENSION FUND	
Ward(s) or groups affected:			
From:		CHIEF FINANCE OFFICER	

RECOMMENDATION(S)

1. Members are asked to note the report.

BACKGROUND INFORMATION

2. The Local Government Pension Scheme (LGPS) is a national scheme providing a range of defined benefits for its members. Southwark Council is an administering body for the LGPS and operates a Pension Fund, investing pension contributions to generate income in order to reduce the cost falling on Council Tax.
3. The amount contributed by staff (6% of pay) is set by statute and does not vary. The Council's contribution is also set by statute and varies depending on the "actuarial" deficit or surplus on the fund. Currently the Council contributes 14.4% of pay.
4. Council Employees and a number of other admitted bodies (e.g. ex Council staff transferred under TUPE) may join the scheme. At 31 March 2003, there were 5,818 active members and 5,563 pensioners (a further 4,127 contributors have deferred pension rights). The market value of the fund was £459m at 30 September 2003. Hewitt Bacon and Woodrow (HBW) are the Fund's actuaries. The WM Company act as the Council's investment advisers.
5. The scheme does not allow for a formal trustee structure. However, the Council activities are covered by the general legislation under the Trustee Investment Act and other legislation. As a part of normal monitoring processes the CFO presents six monthly reports to the Executive, which set out performance and issues relating to investment and fund value. This report follows up on the issues circulated to all Members of the Council on 30 July 2003.

Pension Fund Investment

6. The Council has four external managers who invest funds in accordance with the criteria set out in their individual mandates.
7. Broadly 70% of the Fund's assets are held in equities (44.5% in UK Equities and 25% in Overseas Equities). The remaining 30% is held in a combination of Gilts and Property (4% in Fixed Interest Gilts, 16% in Index Linked Gilts and 10.5% property). Each of the Managers are responsible for a specific part of the portfolio.

8. The table below shows the overall value and the proportion of the fund held by the respective managers in the two quarters to 30 September 2003.

Fund Value	Type of Investment	Value at 30 June 2003	Value at 30 September 2003	Fund %
		£M	£M	
BGI	Passive Equities and Gilts	232.63	239.75	52
Deutsche Asset Management (DeAM)	Active UK Equities	91.90	94.99	21
Putnam	Active Overseas Equities	59.94	63.74	14
Henderson (HGI)	Active Property	60.58	60.79	13
Total Fund		445.04	459.27	100

The current value of the Fund is £ million as at 31 October 2003. (awaiting October information)

Current Performance of Fund Managers

9. Performance is monitored regularly by the Council. The active Managers are expected to “beat” their benchmark by 1% over a rolling 3 year period.
10. In respect of the overall fund, the past year has seen the following returns for the fund as a whole, some 0.4% below the benchmark return.

	Quarter 4 2002	Quarter 1 2003	Quarter 2 2003	Quarter 3 2003	Whole year
Whole Fund	3.7	-2.8	10.0	3.6	14.8
Benchmark	4.1	-3.6	10.7	3.9	15.3
+/-	-0.4	0.8	-0.7	-0.3	-0.4

Individual managers performance against their benchmarks is set out below.

		Quarter 4 2002	Quarter 1 2003	Quarter 2 2003	Quarter 2003	Whole year
BGI	Fund	3.4	-2.6	9.4	3.1	13.6
	Benchmark	3.3	-2.8	9.6	3.0	13.6
Relative return	+/-	0.1	0.2	-0.2	0.1	-0.1
Putnam	Fund	4.4	-4.0	12.6	6.3	19.9
	Benchmark	4.3	-4.5	13.8	7.8	22.2
Relative return	+/-	0.2	0.5	-1.1	-1.4	-1.9
DeAM	Fund	5.9	-6.9	14.3	3.6	16.7
	Benchmark	5.6	-7.2	14.5	3.9	16.7
Relative return	+/-	0.2	0.3	-0.2	-0.3	0.0
HGI	Fund	1.6	3.1	4.2	2.9	12.3
	Benchmark	2.4	2.0	2.7	2.4	9.8
Relative return	+/-	-0.8	1.1	1.5	0.5	2.2

11. Any under-performance of managers is continually monitored. Over the last quarter the fund return was 0.3% below the benchmark. Putnam was 1.4% below the Benchmark, due to stock selection, and below benchmark performance in Europe and Japan. Officers are concerned about Putnam's performance and are currently in discussion with this manager on ways to improve.

Asset-Liability Study

12. In May 2002, HBW carried out a detailed Asset-Liability study following the triennial valuation at 31 March 2001. The report examined the fund's long term liabilities and considered how these might change over the longer term. It recommended the optimum investment strategy to maximise the return to the fund and minimise the risks. The next study will be carried out in 2004 following the formal triennial valuation of the fund.

13. The strategy recommended by the report was that the current asset allocations should be changed to hold fewer UK Equities and more Overseas Equities. Also, the allocation to Index Linked Gilts should be reduced and the fund should start to invest in Corporate Bonds.

14. The recommended allocation is set out below. The table compares the current strategic allocations with these proposals and the actual allocations at 31 March 2003.

	Existing Strategic Allocations	Asset/Liability Recommended Strategic Allocation	Actual position at 31 March 2003.
UK Equities	44.5%	35%	41%
Overseas Equities	25%	35%	21%
Fixed Interest Gilts	4%	5%	5%
Index Linked Gilts	16%	5%	17%
Property	10.5%	10%	14%
Corporate Bonds	Nil	10%	Nil
Cash	Nil	Nil	2

15. The CFO is currently moving the pension investment portfolio to the Asset/Liability recommended strategic allocations. Legal advice has been received on the changes needed to agreements to activate this change and a planned programme is now in action to move to the new set benchmark.

Funding Position

16. Since the last report the Council has received advice on the funding position as at 24 September 2003. The advice was provided by the actuaries, Hewitt Bacon & Woodrow. A copy is attached at Appendix B.

17. The last valuation of the Fund was carried out as at 31 March 2001. The valuation revealed that the Fund had a deficit of £31.6m and contribution rates were set with a view to restoring the solvency level of the Fund to 100% over a period of about 10 years. The next valuation of the Fund is due as at 31 March 2004.

18. HBW have noted that the funding level decreased during early 2003, however due to recent improvements some of the losses have been regained. HBW feel the way forward is to strike the appropriate balance between the funding level considerations and affordability in the short term. In the meantime, the Borough may wish to consider whether any action should be taken to increase contributions to the Fund. Given that this year's budgets will already have been set, HBW do not think it a reasonable expectation that any additional employer contributions are made before 1 April 2004.
19. The new rates emerging from the 2004 valuation are not effective until 1 April 2005 the Borough may wish to consider additional employer contributions over the period 1 April 2004 to 31 March 2005. If employers wish to make additional contributions on a voluntary basis HBW would have no objections on actuarial grounds. The CFO will advise on this matter in the budget report to the December Executive.
20. HBW suggest that a decision on this be deferred until nearer to the valuation date as conditions may alter markedly over the intervening period. It may be appropriate to assess the position at the time that budgets for 2004/05 are being drawn up.

Socially Responsible Investment (SRI)

21. The Executive have requested a report to them on the issue of SRI. Recently the Council has obtained legal advice on this. Officers are seeking clarification of this advice and a further report will be submitted once this has been received.

BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
Investment Manager Reports from BGI, DAM, HGI and Putnam Investors. HBW reports on SRI, SIP, Asset-Liability Study and correspondence.	FMS	Dave Howes Ext : 54314

APPENDIX A

Audit Trail

37. FMS attaches this section in the report for Audit trail.

Lead Officer	Keith Brown	
Report Author	Dave Howes	
Version	Final	
Dated		
Key Decision?	No	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER		
Officer Title	Comments Sought	Comments included
Borough Solicitor & Secretary	No	No
Chief Finance Officer	Yes	Yes
List other Officers here		
Executive Member	Yes	Yes
Date final report sent to Constitutional Support Services		