Pension Fund Committee

Minutes of the meeting held at County Hall, Colliton Park, Dorchester, Dorset, DT1 1XJ on Wednesday, 28 February 2018

Present:
John Beesley (Chairman)
Andy Canning, Tony Ferrari, Spencer Flower, Colin Jamieson, May Haines, John Lofts and Andrew Turner (Scheme Member Representative).

Officer Attendance: Richard Bates (Chief Financial Officer), David Wilkes (Finance Manager - Treasury and Investments) and Karen Gibson (Pensions Administration Manager).

Manager and Advisor Attendance
Alan Saunders, Independent Adviser
Perry Noble, Hermes Investment Management
Claire Peck, JP Morgan Asset Management
Monique Stephens, JP Morgan Asset Management

(Notes:These minutes have been prepared by officers as a record of the meeting and of any decisions reached. They are to be considered and confirmed at the next meeting of the Pension Fund Committee to be held on **Thursday, 21 June 2018**.)

Apologies for Absence
1 An apology for absence was received from Peter Wharf (Vice-Chairman) (Dorset County Council).

Code of Conduct
2 There were no declarations by members of any disclosable pecuniary interests under the Code of Conduct. However, Councillor John Lofts informed the Committee with regard to agenda item 5, Manager presentation from Hermes, that he was in receipt of a pension from the BT Pension Scheme, the owner of Hermes Investment Management. Councillor May Haines also informed the Committee with regard to agenda item 5 that she was in receipt of a pension from Goldman Sachs who managed a fund Hermes were invested in.

Statement by the Chairman
3 The Chairman welcomed Andrew Turner, the scheme member representative, to the Committee.

Minutes
4 The minutes of the meeting held on 23 November 2017 were confirmed and signed.

Public Participation
5 Public Speaking
There were no public questions received at the meeting in accordance with Standing Order 21(1).

There were no public statements received at the meeting in accordance with Standing Order 21(2).

Petitions
There were no petitions received at the meeting in accordance with the County Council's Petition Scheme.

Manager Presentation from Hermes

6 The Committee received a report from Perry Noble, Hermes Investment Management, one of the Fund's two infrastructure managers. Mr Noble described 2017 as a challenging but solid year with more selling than buying of assets but he expected to see more purchases than sales in 2018.

Mr Noble highlighted the current political scrutiny of regulated assets, particularly the water sector. He foresaw significant increased scrutiny of those assets, therefore, Hermes would continue to engage with companies and stakeholders. Continued volatility was predicted as market expectations moved with developments in Brexit negotiations, but infrastructure assets were less likely to be influenced by the outcome of Brexit than other asset classes such as equities.

Members asked if there was an exit strategy should water companies be re-nationalised. Hermes had already reduced their holdings in water companies and anticipated continuing to do so. Investor compensation was the biggest concern and unknown with any nationalisation, as there was very little recent precedent for solvent nationalisations. The UK had reciprocal agreements with other countries that stated compensation for any nationalisation of companies must be at fair value. It was difficult to foresee UK investors compensated less favourably than foreign investors.

A member asked what steps were being taken to mitigate market volatility as Brexit negotiations progressed. Hermes would seek to de-risk by looking closely at individual investments but Mr Noble felt core infrastructure assets should continue to perform solidly over the long term. The importance of investing in good quality companies with good governance was stressed

The Independent Adviser asked for the calculation of Cash Yield and Internal Rate of Return (IRR) to be clarified. Cash Yield included the return of capital and income, of which income had contributed approximately two thirds of the return, and IRR was subject to independent valuation.

The Fund Administrator asked how the realisations from sales of assets had compared to their valuations prior to disposal. Mr Noble replied that overall proceeds from assets had been pretty consistent with their valuations.

The Chairman enquired about the pipeline for new investment opportunities. Mr Noble did not see thematic opportunities in the market but instead he believed there would be proprietary opportunities to build on investments in companies Hermes already knew well. 'Value Added' opportunities were not easy to find, and would require Hermes to look further afield.

A member asked if Hermes could invest in its parent company, BT. Mr Noble confirmed that it could not.

Noted

Manager Presentation from JP Morgan

7 The Committee received a report from Claire Peck and Monique Stephens, JP Morgan Asset Management (JPM), the Fund's emerging market equities' manager. The manager's approach was summarised as looking for "cheap assets with positive trends" i.e. 'value' and 'momentum' stocks. Quantitative screening techniques were combined with fundamental 'bottom up' analysis of individual companies.

The overweight position against the benchmark in commodities and underweight position in defensive stocks positioned the fund to benefit from a cyclical recovery in emerging markets. This recovery was expected for both supply side (cuts in capacity, particularly in China) and demand led (continued global economic growth) reasons.

Geographically, the fund was overweight in Russia and Turkey, and neutral in China, after many years being overweight. However restrictions on foreign ownership of Chinese ‘A’ class shares were expected to be eased, which would open up many more opportunities for investment.

JPM believed that headwinds had turned to tailwinds and that emerging markets were in a “sweet spot” of growth without inflation, coupled with relatively cheap currencies positioned against a weakening US dollar.

It was asked where emerging markets were in the economic cycle, when were they expected to dip again, and what actions would JPM take to protect gains when this came. JPM believed that emerging markets were early, moving to mid, cycle, unlike developed markets that were late cycle, but warned that in-year corrections could be very high even when average returns were growing.

One member asked how JPM future proofed their investment selection process. It was acknowledged that the quantitative screens were reliant on historic data, but were continually tested and challenged. Also the process was coupled to in-depth analysis of individual companies and other proprietary data.

The Fund Administrator asked when frontier markets were upgraded to emerging market status. Ms Peck explained that the status of the domestic stock market was usually the determining factor. There had been two recent upgrades from frontier to emerging market status, Qatar and the United Arab Emirates (UAE), with Saudi Arabia’s status under review.

It was asked whether any emerging markets were expected to be upgraded to developed market status, for example South Korea or China. No upgrades were anticipated in the near future, but South Korea was the closest, with China still some way off. It was highlighted that if South Korea was upgraded to developed market status then China would account for the vast majority of the emerging markets index.

<u>Noted</u>

Independent Adviser's Report

8 The Committee considered a report by the Independent Adviser that gave his views on the economic background to the Fund’s investments, and the outlook for different asset classes.

The US economy looked good but with close to full employment there was concern that recent taxation cuts could be inflationary and therefore markets anticipated interest rate rises. Growth in the UK had been reasonable but held back a little by Brexit uncertainties and was less than in Europe. Growth in Japan was low, and held back because the labour force was not expanding.

Market sentiment in equites was still quite stable, bond yields had not moved up as expected, and property had performed more strongly in 2017 than predicted. In credit markets there were some signs of deteriorating quality of loans, with a number of recent corporate failures. In 2017 sterling had performed strongly against the US dollar, but the Euro had been the strongest performing major currency.

One member raised concerns that US treasury market yields could go up significantly, potentially as high as 4.0%, which might feed through into lower equity prices. The Independent Adviser agreed that an increase of this magnitude would be a concern but, although possible, it was outside market expectations.

Noted

Fund Administrator's Report

9 The Committee considered a report by the Pension Fund Administrator on the asset allocation, valuation and overall performance of the Fund's assets up to 31 December 2017.

The Fund underperformed its benchmark over the financial year to 31 December 2017 by 0.6% but continued to outperform its benchmark over the longer term, with the short term underperformance largely driven by currency movements. The performance of UK equites had been reasonable, and all three global equities managers were now slightly ahead of their benchmarks since inception in December 2015. The Fund's holdings in corporate bonds had been reduced in line with the revised strategic asset allocation but had performed reasonably well.

Recent property transactions were highlighted - the sale of 131 Great Suffolk Street, London for £4.9m, the purchase of Greenford industrial estate, West London for £8.4m and the completion of the purchase of a portfolio of four public houses and a restaurant in Central London for £14.6m.

The Independent Adviser gave an update on the re-negotiations with Insight Investments, the Fund's Liability Driven Investment (LDI) manager. A reduction in base fees had been agreed and was expected to save approximately £200k annually. Discussions continued to agree an updated benchmark and revised performance fee mechanism to better incentivise performance, and also improvements to reporting were sought.

Resolved

1. That the activity and overall performance of the Fund be noted.
2. That the progress in implementing the new strategic asset allocation be noted.
3. That the revised Investment Strategy Statement (ISS) be approved for publication on the Fund's website.

The Brunel Pensions Partnership - Project Progress Report

10 The Committee considered a report by the Fund Administrator on the progress to date in implementation of the Full Business Case (FBC) for the Brunel Pension Partnership (BPP), as approved by the Committee at its meeting on 9 January 2017.

Members were informed that work to establish Brunel Ltd was very well advanced and the Chairman highlighted the Key Measures of Success in the report.

The final specifications of the portfolios for the client funds to invest in had been produced by Brunel Ltd, after review by both the Client Group and the Oversight Board. The majority of the asset classes the Fund invested in 'map' directly to a Brunel portfolio but further details of the smart beta global equities portfolio were needed. Also, there was not a UK specific smaller companies' equities portfolio, but there was a global equivalent that offered a much broader opportunity set.

An engagement session with Matthew Trebilcock, Client Services Director, Brunel Ltd, was held on 28 February 2018 for members of the Fund's Pension Fund Committee and Local Pension Board. Dawn Turner, Chief Executive Officer, Brunel Ltd, had accepted an invitation to attend the Committee's training day in London on 20 June 2018.

Resolved

1. That the progress establishing the Brunel Pension Partnership be noted.
2. That the Fund's indicative asset allocation to the proposed Brunel portfolios be approved.

Pension Fund Administration

11 The Committee considered a report by the Pension Fund Administrator on the administration of the Fund.

Officers updated the Committee that at the date of the meeting, responses to existence checks had not been received from 19 pensioners believed to be living overseas. The next step would be for those pensions to be suspended until proof of existence could be provided.

A member asked if there was any impact for Local Government Reorganisation (LGR) on the proposal to cease all abatements (except in relation to ill health retirement). Officers felt that abatement could dissuade some recipients of pension benefits to return to work, therefore removal of abatement could widen the pool of skills and knowledge available to employers. This could be particularly beneficial at a time of change such as LGR.

Resolved

1. That the update on operational and administration matters relating to the Fund be noted.
2. That the change to the abatement policy be approved.

Treasury Management Strategy 2018-19

12 The Committee considered a report by the Fund Administrator setting out the Treasury Management Strategy (TMS) for 2018-19. Officers explained that the TMS for 2018-19 was unchanged from the TMS for the current financial year and was the same as for the County Council, with some different limits to reflect the different expected cashflows.

Resolved

That the Treasury Management Strategy for 2018-19 be approved.

Dates of Future Meetings

13 **Resolved**

That meetings be held on the following dates:

20/21 June 2018	London (to be confirmed)
17 September 2018	County Hall, Dorchester
21/22 November 2018	London (to be confirmed)

Questions

14 No questions were asked by members under Standing Order 20(2).

Meeting Duration: 10.00 am - 1.00 pm