WILTSHIRE COUNTY COUNCIL **AGENDA ITEM NO. 12**

WILTSHIRE PENSION FUND COMMITTEE
20 June 2007

IMPLEMENTATION OF NEW INVESTMENT MANDATES AND REBALANCING OF FUND

Background & Purpose of the Report

1. At meetings held on 17, 19 and 25 April, Members resolved to appoint Fauchier Partners (Long-Short Equity), Record Currency Management (Currency) and Edinburgh Partners (Global Equity). Good progress is being made towards implementation on 1 July 2007, but a small technicality has arisen that requires a resolution from Members to resolve.

2. The imminent implementation of the new investment strategy means it is also necessary to revisit the rules for keeping the size of the various investment portfolios close to their strategic allocations. Members last considered this matter in February 2003 when the structure was quite different.

Main Considerations for Members

Appointment of New Managers

3. Officers have now largely completed the detailed considerations with the prospective managers and our consultations on the nature of the three new mandates and have concluded that:

   a) In all cases a Pooled Fund approach is preferable to a segregated mandate, usually for administrative reasons, but sometimes for financial reasons too. The proposed Funds are the Jubilee Absolute Equity Fund (Fauchier Partners), the Record Currency Alpha Cash Plus Fund and the Edinburgh Partners Opportunities Fund.

   b) In all cases a flat fee approach is preferable to a performance fee. For all three managers the breakeven point on the performance fee meant that the underperformance would have to be very severe before the performance fee became cheaper.

4. As a result of pursuing the Pooled Fund approach for all three investment managers, a technicality arises, which is that the Fund is effectively buying units in a pool under a Prospectus Agreement, rather than having a direct Investment Management Agreement in place with the manager himself. There is very little practical difference from the Fund's point of view – the best analogy is a corporate finance director acting for his company in one capacity and sitting as a trustee on the company's pension fund in a separate capacity.

5. However, our advice is that in order to follow "due process", Officers now need fresh resolutions from the Committee in relation to investing in these three Funds, rather than appointing three managers. From a practical point of view for the Committee, nothing changes - you will get the products and managers that tendered and presented to you.

Rebalancing of the Fund

6. Moving onto Rebalancing of the Fund, differential movements in the value of the various investment classes that the Fund holds, as well as differences in the performance achieved of the investment managers, make it inevitable that the actual positions within the Fund will vary from their target allocations.

7. The aims of rebalancing are:

   a) Primarily, to maintain the Fund's allocation close to the policy position of 52.5% Equities, 17.5% Bonds, 17% Alternatives and 13% Property. Within Equities, it is important to ensure that the Overseas/UK proportionate allocation (60:40) remains roughly correct, as well as maintaining broadly the correct allocation within Alternatives of 10% Income Yield Equities, 5% Long-Short Equities and 2% Currency.

   b) Secondly, to make sure that each manager and mandate (particularly the smaller ones) does not drift too far from its target allocation, because these manager allocations were also set for specific reasons.

8. However, given the specialist individual mandates that the Fund now has for much of its strategy, these primary and secondary aims of rebalancing largely lead to the same conclusion, notably a need to keep each mandate reasonably close to its target allocation.

9. The task of keeping the Fund in balance should continue to be largely achievable through the allocation of the Fund's positive monthly cashflow of £1m - £2m, as has been the case for the last 4-5 years. This is done by allocating the new cash to the most under-weight mandate. In doing this, no attempt is or should be made to make tactical asset decisions based on estimates of the likely performance of certain markets or managers; it is a purely mechanical process.

10. Nevertheless, with the volatility prevalent in stock markets, it is very likely that at some point in the future, some positive rebalancing action will be required at some point. If the values are relatively small, this can be managed in-house, but in certain circumstances it might be appropriate to use the Fund's Custodian (currently ABN AMRO Mellon) or even its transition manager (currently Lehman Brothers) to execute the rebalancing as cost effectively as possible.

11. Previously the County Treasurer had delegated authority from this Committee to carry out rebalancing, if required, and it is proposed that this delegation now be given to the Chief Financial Officer. Any use of this delegated power would be reported to a future meeting of the Committee.

12. The Appendix gives the proposed approach to keeping the Fund balanced and sets out suggested tolerances within which individual asset classes and ranges can move before rebalancing is initiated, following consultations with the Fund's investment consultants at Hymans Robertson.

Financial Implications and Risk Assessment

13. It is necessary to balance the desire to keep close to the Fund's Investment Strategy (so as to avoid reduced returns or higher volatility) with the need to avoid frequent rebalancing, which might incur significant costs (eg. administration, commission, tax,

bid-offer spreads, etc). Therefore, rebalancing will be done as infrequently as possible and only when one or more of the limits set out in the Appendix are breached.

Environmental Impact of the Proposal

14. There is none.

Proposal

15. The Committee is asked to:

a) approve that officers conclude an investment of 5% of the Wiltshire Pension Fund in the Jubilee Absolute Equity Fund from 1 July 2007 (this rescinds minute 17 b) of the meeting of this Committee on 17 April 2007);

b) approve that officers conclude an investment of 2% of the Wiltshire Pension Fund in the Record Currency Alpha Cash Plus Fund from 1 July 2007 (this rescinds minute 20 b) of the meeting of this Committee on 19 April 2007);

c) approve that officers conclude an investment of 7.5% of the Wiltshire Pension Fund in the Edinburgh Partners Opportunities Fund from 1 July 2007 (this rescinds minute 23 b) of the meeting of this Committee on 25 April 2007);

d) note that all three mandates will be on the basis of flat not performance fees;

e) approve the Rebalancing Rules for the Fund's investment portfolios as proposed in this report; and

f) delegate authority for implementation of the Rebalancing Rules to the Chief Financial Officer.

SANDRA SCHOFIELD
Chief Financial Officer

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Unpublished documents relied upon in the production of this report: NONE

93/2007/WPF/DB

APPENDIX

WILTSHIRE PENSION FUND INVESTMENT - REBALANCING RULES FROM 1 JULY 2007

APPROACH

1 The task of keeping the asset classes and managers/mandates in balance should continue to be largely achievable through allocation of the Fund's positive cashflows of £1m-£2m per month, with the aim of keeping each asset class and manager/mandate as close to its target allocation as possible.

2 If this is not possible, positive rebalancing will take place by taking money from the most overweight asset classes and managers/mandates and giving it to the most underweight ones, but this will not be done more than quarterly and only then if there is an actual breach of one or more of the limits. Frequent rebalancing is undesirable due to the transaction and administration costs involved.

3 No attempt will be made by the Chief Financial Officer to make tactical asset decisions to feed into either the allocation of the monthly cashflow or any rebalancing exercises.

LIMITS

The proposed upper and lower limits are shown below:

LIMITS ON ASSET CLASSES	*Lower Limit*	**Target Allocation**	*Upper Limit*
Equities:			
UK	*19.0%*	**20.5%**	*22.0%*
Overseas	*30.5%*	**32.0%**	*33.5%*
Total Equities	*49.5%*	**52.5%**	*55.5%*
Bonds	*15.5%*	**17.5%**	*19.5%*
Property	*11.0%*	**13.0%**	*15.0%*
Alternatives (AIG/Currency/Long-Short)	*15.0%*	**17.0%**	*19.0%*
TOTAL	*91.0%*	**100.0%**	*109.0%*

LIMITS ON MANAGERS & MANDATES	*Lower Limit*	**Target Allocation**	*Upper Limit*	
Capital International - Core UK & Overseas	*17.0%*	**19.0%**	*21.0%*	
Capital International - AIG	*8.0%*	**10.0%**	*12.0%*	
Baillie Gifford - Core UK	*10.5%*	**12.5%**	*14.5%*	
Baillie Gifford - LTGG	*10.5%*	**12.5%**	*14.5%*	
Western Asset Management	*15.5%*	**17.5%**	*19.5%*	
ING Real Estate	*11.0%*	**13.0%**	*15.0%*	
Edinburgh Partners	*6.5%*	**7.5%**	*8.5%*	
Fauchier Partners	*4.0%*	**5.0%**	*6.0%*	The initial allocation will be around £58 million (5%). Under the terms of the mandate, this amount will be effectively locked in for 3 years, so if the overall Fund value fell below £967 million (ie. £58m / 6%) in that time, the upper limit would be breached and need reviewing with the Committee.
Record Currency Management - Active	*1.5%*	**2.0%**	*2.5%*	
Record Currency Management - Passive (underlying cash equitised against FTSE100 Index)	*0.0%*	**1.0%**	*2.0%*	In periods where there have been extreme movements in currency markets, it might be necessary for the allocation to go above 2% for a short period to allow the manager to settle maturing contracts and to retain a cash buffer for the next period. However, if it did happen, the Chief Financial Officer would report to the Committee at the earliest opportunity. Past history suggests that an allocation of 1% will be sufficient in most market conditions.
TOTAL	*84.5%*	**100.0%**	*115.5%*	