

WIRRAL COUNCIL

PENSIONS COMMITTEE

1ST JULY 2014

SUBJECT:	<i>EUROPEAN EQUITY MANDATE – RESULT OF TENDER EXERCISE</i>
WARD/S AFFECTED:	<i>ALL</i>
REPORT OF:	<i>STRATEGIC DIRECTOR OF TRANSFORMATION & RESOURCES</i>
KEY DECISION	NO

1.0 EXECUTIVE SUMMARY

- 1.1 The purpose of this report is to present to Members the recommendations of officers concerning the appointment of investment managers to a European (ex UK) equities mandate for Merseyside Pension Fund.
- 1.2 The appendices attached to the report contains exempt information. This is by virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972 i.e. information relating to the financial or business affairs of any particular person (including the authority holding that information).

2.0 BACKGROUND AND KEY ISSUES

- 2.1 Members, at their meeting on 20th January 2013, approved a plan to carry out a public tender exercise, commencing early in 2014, to appoint investment managers to an active, unconstrained European (ex UK) equities mandate. That process has been successfully concluded, culminating in recommendations to appoint two managers to the mandate, as out-lined in the Appendices to this report.
- 2.2 European (ex UK) equities comprise 8% of the Fund's strategic benchmark. In line with the Fund's investment strategy, 5.5% of the Fund's assets are to be allocated to external investment managers, pursuing strategies that seek to out-perform the FTSE World Europe (ex UK) index over an appropriate time horizon. JLT were called-off from the Fund's Investment Manager Selection Consultants Framework to carry out a search process, under direction from Fund officers, which would deliver on our strategic objectives and be fully compliant with the Council's Contract Procedure Rules. Details of the process and its outcomes are set out in JLT's report, which is presented in the Appendices to this paper.
- 2.3 JLT were given a specific brief to carry out the final stage of evaluation of investment manager submissions in a manner consistent with the Fund's views on active management and signifiers of investment manager skill. Their process (which we have used for prior manager search exercises) sought, in particular, to identify forward-looking indicators in managers' submissions, such that might give a degree of confidence in managers' ability to add future value,

for a reasonable cost. Therefore, the final evaluation (following assessment of all submissions and further clarification discussions with officers) was carried out by applying the formula:

Probability of achieving outperformance x outperformance target (net of fees)

- 2.4 The most recent valuation of the Fund's assets would put the overall size of this mandate at £347 million. The recommendation is to evenly divide this mandate between the two managers identified in the JLT report.

3.0 RELEVANT RISKS

- 3.1 There is an accepted body of evidence that describes any number of pitfalls that can befall pension funds when selecting active investment managers. The evidence describes the tendency for pension funds to appoint investment managers after a period of good performance who then go on to under-perform; and to terminate managers for under-performance who then subsequently go on to out-perform. This arises due to the tendency to over-rely on assessing past performance as a basis for predicting which managers will be successful generators of alpha (risk-adjusted outperformance relative to a specified benchmark index). This leads to problems of herding and selection bias, as well as overlooking the phenomenon of mean reversion.

It should be possible, using a mixture of quantitative and qualitative analysis, to develop a manager selection model that corrects for these problems and seeks to pinpoint evidence of alpha-generating ability using appropriate forward-looking indicators. Officers are confident that the process supported by JLT has delivered this.

- 3.2 The method for including an assessment of fee proposals (on the basis of a net return) was determined to be the most appropriate for establishing the most economically advantageous tender in this context, in line with the Council's procurement policy and OJEU requirements. Support from the Corporate Procurement Team and the use by JLT, at all stages of the process, of The Chest online portal ensured proper maintenance of a control environment and audit trail through-out.

4.0 OTHER OPTIONS CONSIDERED

- 4.1 None

5.0 CONSULTATION

- 5.1 None

6.0 IMPLICATIONS FOR VOLUNTARY, COMMUNITY AND FAITH GROUPS

- 6.1 None

7.0 RESOURCE IMPLICATIONS: FINANCIAL; IT; STAFFING; AND ASSETS

7.1 The full cost of the exercise will be borne by the successfully appointed investment managers, upon commencement of their mandate. JLT will provide detailed feedback (upon request) to any of the unsuccessful managers, at no charge. This 'manager pays' remuneration model is increasingly becoming the industry norm for consultant-led active manager searches of this nature.

8.0 LEGAL IMPLICATIONS

8.1 None

9.0 EQUALITIES IMPLICATIONS

9.1 Has the potential impact of your proposal(s) been reviewed with regard to equality?

(b) No because there is no relevance to equality.

10.0 CARBON REDUCTION IMPLICATIONS

10.1 None

11.0 PLANNING AND COMMUNITY SAFETY IMPLICATIONS

11.1 None

12.0 RECOMMENDATION/S

12.1 That Members approve the recommendations for the appointment of managers, as set out in the JLT report.

13.0 REASON/S FOR RECOMMENDATION/S

13.1 The investment management contracts for the externally-managed active European ex-UK equity mandate were required to be publicly tendered. A robust and compliant process has taken place, resulting in clear recommendations.

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APPENDICES

Exempt Appendix 1 – Officer recommendations arising from European ex-UK equity manager search

Exempt Appendix 2 – Merseyside Pension Fund, European ex-UK Equity search: Mandate Award Proposal (report of JLT)

REFERENCE MATERIAL

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
Pension Committee	20th January 2013