Notice of Meeting

Surrey Pension Fund Board

Date & time	Place	Contact	Chief Executive
Friday, 14 November 2014 at 9.30 am	G30, County Hall, Kingston upon Thames, Surrey KT1 2DN	Cheryl Hardman Room 122, County Hall Tel 020 8541 9075 cherylh@surreycc.gov.uk	David McNulty

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This meeting will be held in public. If you would like to attend and you have any special requirements, please contact Cheryl Hardman on 020 8541 9075.

Elected Members

Ms Denise Le Gal (Chairman), Mr Nick Skellett CBE (Vice-Chairman), Mr W D Barker OBE, Mr Tim Evans, Mr John Orrick and Mr Stuart Selleck

Co-opted Members:

Mr Tony Elias (District Representative), Judith Glover (Borough/District Councils), Ian Perkin (Office of the Surrey Police and Crime Commissioner) and Philip Walker (Employees)

AGENDA

6	**MANAGER ISSUES AND INVESTMENT PERFORMANCE** This report is a summary of all manager issues that need to be brought to the attention of the Pension Fund Board, as well as manager investment performance.	(Pages 1 - 6)

David McNulty
Chief Executive
Published: 11 November 2014

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Annex 6

Notes from Meetings with Fund Managers: 7 November 2014

Hosted by Standard Life

Manager	**Attending**
UBS	Digby Armstrong Steve Magill
Marathon	Graeme Neuff
Standard Life	Dale MacLennan Neil Richardson
Majedie	Simon Hazlitt

6 **UBS**

1. Met with Digby Armstrong and Steve Magill from UBS.

2. UBS discussed the arrangements of the current value-oriented approach, which has a total of ten clients with six local authorities, and the average holding period for the local authorities is 20 years. This allows the value investment team to take a long term view of the market.

3. Despite the long term approach, UBS were keen to explain the reasons for a weaker performance over the past year, relative to the benchmark.

4. The very strong performance over the previous three years compared to the benchmark was driven largely by undervalued cyclical mid cap stocks which have fallen out of favour over the last nine months. UBS have sought to shift the portfolio to a more defensive footing with a focus on cheap large cap companies with stable earnings flows.

5. The current portfolio positioning is now broadly in line with the overall index weighting for small, mid and large caps.

6. The largest detractor to overall performance was from not holding any shares in the pharmaceutical company, Shire, whose price shot up following takeover rumours, although it has fallen back since the US government raised the rhetoric on so called tax inversion deals.

7. Another significant negative impact was the long term holding of Balfour Beatty. Recent problems in the UK construction industry have led to two consecutive profit warnings. UBS took the opportunity to add to the stock following this latest share price decline.

8. UBS were overweight the clothes retailer, N Brown, who reported a fall in profit, which was attributed to the warmer weather, thus limiting high margin coat sales. UBS remain confident in the stock with its niche market position and expanding online sales.

9. UBS were questioned regarding their recent purchases of Tesco stock which began prior to the accounting scandal. The justification for investing was around the potential for new management and could result in a focus on maintaining sales margins. In response to questions on potential litigation, UBS were not over concerned about the impact, given the size of Tesco and saleable assets. Litigation costs would likely be absorbed without too much trouble

10. UBS sold the reasonable position of Standard Chartered Bank after losing confidence with the management and the shareholder votes against its remuneration policies. This was before a recent slide in the Standard Chartered share price. The proceeds were used to fund an investment into HSBC with a similar geographical focus to that of Standard Chartered.

11. In response to questioning on the portfolio exposure to Europe, UBS claimed that it was roughly in line with the index exposure.

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Marathon

1. Met with Graeme Neuff from Marathon.

2. In response to questioning on Japan, given the sizable fund holdings in Japan (15%) and recent Bank of Japan liquidity actions, Marathon were keen to stress that their investment case for certain Japanese equities is not affected by the recent unexpected decision to expand QE purchases.

3. The positive steps in terms of corporate governance and shareholder focus has continued with some Japanese stocks seeming more like western stocks in that regard.

4. Marathon then went on to discuss the large currency risk that the divergence in central bank policy between UK, US and Japan might result in. Marathon have not taken currency into account in an investment case as it is not considered their core strength, but in the case of the large Yen exposure they are considering implementing a rolling hedge.

5. The extent to which the Yen exposure will be hedged is not yet determined, but it will be not to create a fully neutral position. The planning is still at an early stage. Officers will be contacted prior to any implementation.

6. In response to questioning on the driver for this currency option, Marathon said that it was not a client driven decision to appease US investors, but a management fear over the Yen and the decoupling of South East Asian currency with US Dollars.

7. Key drivers of performance over the past year were Intel Corp which benefited significantly from the market overestimating the decline of ‘old tech’. Intel produce a significant number of chips for the PC market. The chip market requires substantial capital investment and this significantly limits the potential for market completion. IBM have recently sold their chip business to avoid this large ongoing expenditure.

8. Other strong performers over the period were advanced medical manufacturers, Sigma Aldrich and Coloplast. Sigma Aldrich provides high tech lab equipment where market quality is more important than price. Sigma stock was the beneficiary of a recent bid offer.

9. Coloplast have been included within the portfolio for the last 20 years and is currently seen as a touch expensive, but Marathon are keen to retain the exposure as they do not want to limit their influence and access to the company as well as a potential reduction in research that would accompany a lower stock position.

10. Marathon are overweight in the family run insurer/investor, Alleghany, who follow a similar model to that of Berkshire Hathaway run by Warren Buffet, in which insurance premiums are used to fund investment in other enterprises. Of particular interest was a slightly speculative position for Alleghany where the attractive selling point is a technology which allows for significant exploitation of old oil wells.

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Standard Life

1. Met with Dale MacLennan and Neil Richardson from Standard Life (SL) to discuss the first full quarter of the Global Focused Strategies Fund (GFS).

2. SL had expanded the multi asset team working on the GFS to allow for greater analysis of particular investment strategies. The limited size of GFS relative to GARS allows for more detailed liquidity constrained portfolio ideas, with use of the individual security research which comes from other areas of the wider SL team.

3. The fund performance for Surrey since inception (17 June 2014) to 30 September 2014 was -0.6%.

4. The fund is subject to stress test scenario planning in order to manage the potential drawdowns to the fund. The recent market volatility was seen as a useful demonstration of the real life application that back testing and paper portfolios were not able to realise, the result of which was that not one of the 35 separate strategies failed during the period.

5. One area of focus was Japanese real estate. Vacancy rates have been declining as confidence in the Japanese economy started to make some slight progress. A key driver of strong returns was the high rental rate over and above the cost of capital. The sector has also seen strong asset flows back.

6. The fund has also focused upon the heavy discount applied to European investment banks. All European investment banks now comply with the same rules and good results in recent stress tests imply more stable banks.

7. The major litigations arising from the banking crisis have largely worked their way through the system or large class action provisions have already been made. The currency exchange litigation is likely to still be sizable. SL suggested that the current aggregate valuation of banks in the sector is limited to the extent that the investment banks are heavily discounted to far too much a degree. Whilst SL were not expecting bumper returns from investment banks, it did think they would outperform the rest of the market.

Majedie

1. Met with Simon Hazlitt from Majedie.

2. Majedie further continued the progression to majority staff ownership with the company using assets to buy shares back from the original capital backing, thus allowing for a smaller limited investment fund which can access smaller investment opportunities.

3. Recent positive performance arose from the fund's investment in a small number of international stocks, including the European telecoms sector and Italian banks with strong credit control and exposure to the resilient economy of northern Italy.

4. A negative over the last year was the exposure to M&S with reducing market expectations, but which surprised the markets with good results after the quarter end which showed improved cost and inventory management.

5. Majedie have sold down positions in Royal Dutch Shell and BP following concerns over the falling oil price and recycled some of the proceeds into beneficiaries of the lower oil price, such as International Airlines Group (IAG) and the cruise ship owner Carnival.

6. Majedie is positioned with strong exposure to the healthcare sector and the belief that there is a much larger and stronger drug pipeline coming through. Mejedie is overweight in AstraZeneca with a strong belief in the likely profitability of their immunotherapy section.

7. The cost of genome sequencing has collapsed in recent years, thus allowing for the development of individual targeted drug courses.

8. Majedie is wary over the potential for emerging markets with the expectation that China's official growth rate is not borne out by other indicators such as electricity usage and coal and steel orders. Majedie estimated this growth rate at closer to zero, which will put significant pressure upon nearby economies and key commodity producers. As such, Mejedie is heavily underweight the mining sector.

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