

PENSIONS COMMITTEE – 29 NOVEMBER 2007

PRIVATE EQUITY AND HEDGE FUND MANAGERS

SUMMARY

Representatives from the Council's private equity and hedge fund managers will provide Members with an update of their strategies and performance at this meeting.

This report reminds Members of the background on these investments and provides the latest available information on performance.

REPORTED FOR INFORMATION

1. Introduction

At the November 2005 meeting of the Committee the results of the asset liability study were reported. Members agreed a new asset allocation which included 2.5% allocations to new investments in each of a fund of private equity funds and a fund of hedge funds. Following a selection procedure Partners Group were selected as manager for private equity funds and RMF Investment Management for hedge fund investments.

Each manager will be making a short presentation on the investments they are making for the Fund. Paper copies of the presentations will be circulated to Members prior to the meeting.

2. Hedge Funds

The contract for investment management in hedge funds is with Man Investments Ltd, a UK company regulated by the Financial Services Authority. The funds are invested in "RMF Four Seasons Strategies" a fund run by RMF Investment Strategies Ltd, which is also a Swiss company, but is in turn part of the Man Group plc a FTSE 100 company. This investment covers a wide spread of the different types of hedge fund investment in order to minimise risk.

An investment of £10m was made with effect from 1 September 2006.

The presentation will be made by John Wilkinson (Man Investments Ltd) and John Angell (Senior Portfolio Manager at RMF).

Hedge funds cover a broad spectrum, but are essentially funds invested with managers with the aim of achieving a return above cash, rather than relative to equity or bond markets. They aim to add value in all market conditions and may use the four main asset classes of equities, bonds, currencies and commodities to do this. As such they are regarded as a lower risk investment than equities, and an average annual return of 7% is expected.

Performance figures for October 2006 to September 2007 show a return of 11.1% against a benchmark return of 9.6%. The benchmark is a 7-day cash investment rate

plus 4%. The £10m investment was valued at £11.4m at 31 October 2007. RMF will update Members with their latest returns.

3. Private Equity

Partners Group (UK) Ltd were appointed as fund of funds private equity investment manager. The UK firm is part of the Swiss parent company Partners Group.

The presentation will be made by Mr Stefan Naef (Principal) and his colleague Guy Waller.

The Pension Fund is investing in the “Partners Group Global Value 2006, L.P.” which is targeted at a good spread of investments over Europe, USA and Asia and over different stages and type of investment. The Fund has entered into a commitment amount of €20m (around £13.6m) in order to achieve an eventual cash investment of 2.5% of the Fund. So far Partners Group have drawn funds totalling €6.3m (£4.5m).

Private equity is capital available for investment in unlisted companies, and can be categorised into :-

- Buy-outs/buy-ins of established companies
- Development capital to enable companies to expand
- Venture capital to start or grow a company from an early stage

Investments are of a long term nature and losses are generally expected in the first few years of investment as there are risks that the companies do not succeed. However there is greater return potential in later years – Mercer assumed a long term return of 11% compared to 8.4% from normal equity investment. In order to reduce risk of losses occurring a “fund of funds” approach has been adopted, whereby a share is taken in many funds. This has the advantage of:-

- Low minimum investments
- Diversification
- Access to top tier managers
- Experience and expertise in selecting funds

Performance returns for October 2006 to June 2007 (the latest figures received from Partners Group), as reported by the WM Company, show a return of -9.6% against a benchmark return of +11.2%. These results reflect the expected return profile of private equity investments. If any more up-to-date performance information becomes available this will be reported at the meeting.

4. Summary of Financial Implications

Investment managers’ fees are met by the Pension Fund.

Local Government Act 1972 – section 100d List of background documents

Investment Strategy Review – Mercer Investment Consulting - November 2005
WM Company Performance Review – September 2007

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