

**TYNE & WEAR
PENSION FUND**

**Report & Accounts
1998/99**



**Administered by
SOUTH TYNESIDE METROPOLITAN BOROUGH COUNCIL**

REPORT and ACCOUNTS

1998/1999

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MEMBERS OF THE PENSIONS COMMITTEE, INVESTMENT MANAGERS AND ADVISORS

Committee Members

Chairman	:	Councillor R.S. Haws, J.P.
Vice Chairman	:	Councillor Mrs. S. Stratford
South Tyneside M.B.C.	:	Councillor T.A. Bamford Councillor Mrs. E. Battye Councillor C. Bonnar, J.P. Councillor J.F. Harper Councillor J. Selby Councillor J. Temple Councillor Mrs. L. Waggott
Gateshead M.B.C.	:	Councillor W. Gordon (substitute - Councillor H. Smiles)
Newcastle upon Tyne City Council	:	Councillor G. Bell (substitute - Councillor C. Gray)
North Tyneside M.B.C.	:	Councillor Ms. A. Richardson (substitute - Councillor C.B. Pickard)
City of Sunderland Council	:	Councillor Mrs. L.A.F. Farthing (substitute - Councillor P. Young)
Trade Union Representatives	:	G. Brown - UNISON W. Flynn - UCATT I. Rossiter - RMT

Investment Managers

Balanced Managers :	:	Phillips and Drew Mercury Asset Management (until 9.10.98) Fidelity Institutional Asset Management (from 23.11.98)
Specialist Managers :	:	Morley Fund Management (from 12.11.98)
UK Equities	:	Schroder Investment Management
Japan and Pacific Basin	:	J.P. Morgan Investment Management
North America	:	Capital International
Continental Europe	:	Prudential Portfolio Managers
Global Bonds	:	
Indexation :	:	Barclays Global Investors
Property Manager :	:	Argyll Property Asset Managers
Actuary and Investment Advisor	:	Watson Wyatt Partners
Director of Corporate Services	:	P.J. Haigh

INTRODUCTION

Over 1998/99, the Fund's membership rose by 1,595 to 76,167. This total is comprised of 41,043 contributors, 25,245 pensioners and 9,879 deferred members.

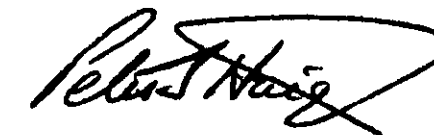
The Fund increased in value by £117 million, from £1,858 million to £1,975 million. The investment return was 6.4%, which was 0.5% below the median U.K. pension fund return of 6.9%.

In order to avoid taking too short term a view of investment performance, pension fund returns are generally assessed over five year periods. This Fund's average annual return over the last five years has been 12.2%, which is comfortably above the rate of inflation and the increase in wages over the period, although it is below the median U.K. pension fund return for the period of 12.5%.

The underperformance over the period has arisen out of the part of the Fund which was under balanced management, which was about two thirds of the total Fund. The Pensions Committee has recognised this situation and has undertaken a review of the investment management structure. The outcome has been an adjustment to the structure to provide for broadly equal amounts of the Fund to be under balanced and specialist management. These revised arrangements were in full operation by January 1999. Further details are given in the Investment Report on page 13.

An actuarial valuation has been carried out in 1998. This had to take account of the removal of the tax credit on U.K. equity dividends, which was announced in the July 1997 budget, and has resulted in an increase to employers' contribution rates. The recommendations arising from this valuation have been implemented from 1st April 1999.

A revised set of regulations came into effect on 1st April 1998. These are the Local Government Pension Scheme Regulations 1997 and they contain a number of enhancements to the current benefits package. They have also standardised the employees contribution at 6% of pay from April 1998, with protection for those on manual grades who were paying 5%.



PETER J. HAIGH
DIRECTOR OF CORPORATE SERVICES

FUND REPORT**ADMINISTRATION**

South Tyneside Metropolitan Borough Council is the administering authority for the local government pension fund for the Tyne and Wear County area. The Fund is set up in accordance with the provisions of the Local Government Pension Scheme.

The Council has established a Pensions Committee which is required to control and resolve all matters relating to the administration and investment of the Fund.

The Committee consists of sixteen members. Nine of the members are nominated by South Tyneside Metropolitan Borough Council, the other four district councils within the County area nominate one member each and three representatives are nominated by the trades unions.

The Committee meets quarterly to consider comprehensive reports covering all aspects of investment activity. Matters of substance relating to pensions administration which require the Committee's awareness or a formal administering authority decision are also considered at these meetings. Additional meetings are called should an aspect of the investment of the Fund require an in-depth review.

The Committee also has an annual meeting at which it considers the Report and Accounts.

Annual meetings are held for the trades unions and for employing organisations. The agenda for these meetings covers the actuarial position, investment performance and benefits structure, and includes presentations by the Actuary and by an investment manager.

The strategy and performance of the investment managers is monitored on an ongoing basis by the Director of Corporate Services.

The administration of matters relating to Fund members' benefits is also undertaken by the Director of Corporate Services.

MEMBERSHIP

As at 31st March 1999, there were 84 employing bodies participating in the Fund. This includes the five district councils and other organisations which provide a public service within the County area. A full list of these organisations is given on pages 10 and 11.

The number of employees contributing to the Fund was 41,043, an increase of 84 over the previous year.

There were 25,245 people in receipt of payments from the Fund. This is an increase of 595 over the previous year.

The remaining group of Fund members are the 9,879 deferred members. These are either former employees who left their employing organisation before retirement age or employees who opted out of the Scheme whilst continuing to be employed. As and when they reach retirement, they are entitled to the payment of pension benefits based on their accrued service.

COMMUNICATIONS STRATEGY WITH FUND MEMBERS

The Fund works with the employing bodies to promote membership of the Local Government Scheme as being in the best interests of employees and strives to communicate effectively with all members. This is achieved by distributing a range of literature and by arranging presentations for members.

A comprehensive selection of information leaflets on specific pension topics is available. Each new employee receives a new starter pension leaflet to advise them about the Scheme. Current members receive an annual newsletter and a members annual report is issued to both current members and pensioners.

LEGAL FRAMEWORK

The provisions of the Local Government Pension Scheme are contained in statutory regulations which are made and amended when necessary by the Department of the Environment, Transport and the Regions and are ultimately approved by Parliament. These regulations apply nationally to all local authorities in England and Wales.

The Local Government Pension Scheme Regulations 1997, which were introduced with effect from 1st April 1998, set out the current rates of contribution and the method of calculation of benefits.

The legal framework for the investment of the Fund is set out in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998. These regulations set out the types of investments which can be made, which include company and government securities, property and unit trusts, and set out restrictions on the proportion of the Fund which can be held in certain types of investment.

EMPLOYEES CONTRIBUTIONS

Since the introduction of the current regulations, all members have paid a common contribution rate of 6%. Prior to this date, manual workers paid 5%. Those manual workers who were members prior to 1st April 1998 will retain the right to pay 5% for as long as they remain in the Scheme.

EMPLOYERS CONTRIBUTIONS AND THE FUND VALUATION

Employees' contributions do not cover the total cost of the benefits. Employers participating in the Fund meet the balance of the cost with their contributions. The Fund's Actuary values the Fund every third year in order to assess each employer's share of the cost.

The employers' contributions for the 1998/99 year were set by the 1995 valuation. In common with the valuations of the majority of local government funds, that valuation had revealed a deterioration in the financial position of the Fund. This was attributable to a range of factors, including changes to the statistical assumptions underlying the valuation, and that the contributions paid over the three year interval period to 1995 were below the level required to maintain the funding level. The deficiency was being made good over the average expected future working lifetime of the district councils' employees in the Fund, which was a period estimated at thirteen years from the valuation date.

The valuation undertaken as at 31st March 1998 has shown that the funding level was 86.7%. This is a decrease of 0.7% from the level of 87.4% revealed by the 1995 valuation. The performance of investment markets over the three year period had been better than that assumed at the time of the 1995 valuation and this was a large positive factor for the funding level. However, this was cancelled out by a range of negative factors, of which the most significant by far was the removal of the tax credit on U.K. equity dividends, which occurred as part of the measures included in the July 1997 budget. The strategy is still to make good this deficiency over a period of thirteen years from the latest valuation date.

The 1998 valuation also revealed that an increase was required to the average future service contribution rates of the district councils. This is the contribution required to meet the cost of the accrual of future benefits. Again, the largest factor behind the increase was the loss of the tax credit on U.K. dividends.

Changes to the employers' contribution rates have been introduced with effect from 1st April 1999. Information on the actuarial position of the Fund and the employers' contributions is set out in the Actuary's reports, which are on pages 18 and 19.

BENEFITS

The Scheme provides its members with an extensive range of guaranteed benefits for employees and their dependants including:

- A pension and tax free lump sum on retirement
- Widows' and widowers' benefits
- Children's pensions
- Index-linking of all pensions
- A lump sum on death in service (and sometimes on death after retirement)
- Transfer values to other pension arrangements or index-linked preserved benefits for early leavers
- A refund of contributions where no other benefit is due
- Facilities for paying additional contributions to provide additional benefits.

ADDITIONAL VOLUNTARY CONTRIBUTIONS

Whilst the Local Government Pension Scheme provides an excellent benefits package, it is normally possible to increase benefits and take full advantage of the tax relief which is available. This can be done either by purchasing added years of service within the Scheme or by paying into an Additional Voluntary Contributions (AVC) plan.

This Fund's AVC plan is arranged with Equitable Life. In addition to allowing members to boost their pension up to the maximum allowed under Inland Revenue rules, it can also be used to provide extra life assurance.

THE 1997 REGULATIONS

The Local Government Pension Scheme Regulations 1997 replaced the previous Scheme regulations with effect from 1st April 1998. In addition to clarifying and simplifying the rules, the new regulations introduced a number of improvements, including those listed below:

- Members may, with the agreement of their employer, retire with reduced benefits at age fifty or over. If the member has reached the age of 60, the employer's permission is not required. Where the aggregate of age and Scheme membership is at least eighty five years, the benefits are not reduced.
- Employers have the ability to augment Scheme benefits (i.e. credit additional service) up to a maximum of six and two third years. Additional awards must be paid for by a payment of a lump sum into the Fund.
- Retirement benefits are guaranteed for five years. In other words, if a pensioner dies within five years of retirement, there will be a payment due to the next of kin equal to five years pension less the amount of pension already paid.
- Widows' and widowers' pensions are payable for life and do not cease upon remarriage or cohabitation.
- An administering authority may decide not to suspend pensions during periods of re-employment. The Pensions Committee has agreed to this condition for pensioners of the Tyne and Wear Fund.
- Employers are able to set up shared cost AVC arrangements in conjunction with the administering authority.
- Employers have the power to waive or reduce contributions for employees with more than forty years local government service.
- At retirement, members may give up part of their pension to provide a higher lump sum, or give up part of their lump sum to provide a higher pension.
- Members who have been paying into the in house AVC scheme may use their accumulated fund to purchase additional service in the main Scheme.
- Although members could always choose the best of their last three years pay for the calculation of pension benefits, this choice could only be exercised if the actual pay for the chosen year was higher than the final year's pay. This restriction has now been removed, and the pay of any of the last three years may be used. If a year other than the final year is selected, the pay is then adjusted in line with inflation. Therefore, a member whose pay has risen at a lower rate than inflation will be better off choosing one of the two years prior to the final year.

CONTACTS

Queries concerning contributions or benefits should be raised with the Communications Team. Their address is the Pensions Office, Civic Centre, Campbell Park Road, Hebburn, NE31 2SR. The telephone number is 0191 424 4141.

Queries concerning the investment of the Fund should be raised with the Head of Loans and Investment. The address is the Town Hall and Civic Offices, Westoe Road, South Shields, NE33 2RL. The telephone number is 0191 424 7000.

ORGANISATIONS PARTICIPATING IN THE FUND

Members as at 31st March 1999
Contributors Deferred Pensioners

METROPOLITAN DISTRICT COUNCILS

Gateshead	6,950	1,428	4,018
Newcastle upon Tyne	8,819	1,879	6,166
North Tyneside	4,997	1,184	2,739
South Tyneside	4,667	1,024	3,045
Sunderland	7,456	2,112	4,944
Sub Totals	32,889	7,627	20,912

OTHER SCHEDULED BODIES

University of Northumbria at Newcastle	1,298	271	357
University of Sunderland	821	184	214
Nexus	900	406	1,093
Northumbria Police Authority	1,504	369	723
Northumbria Probation and After-Care Service	474	87	194
Tyne and Wear Fire and Civil Defence Authority	260	48	131
Tyne and Wear Passenger Transport Authority	117	22	56
City of Sunderland College	311	12	55
Gateshead College	140	41	22
Newcastle College	341	32	109
North Tyneside College	97	7	11
Tynemouth College	34	5	4
South Tyneside College	258	14	49
Wearside College	0	5	47
Birtley Town Council	7	2	1
Monkwearmouth College	0	1	5
Former Tyne and Wear County Council	0	141	246
Former Tyne and Wear Residuary Body	0	10	30
Former North East Regional Airport	0	0	31
Sub Totals	6,562	1,657	3,378

ADMITTED BODIES

Stagecoach Travel Services (Busways)	395	199	401
Newcastle International Airport Company Ltd.	423	80	170
Age Concern Newcastle	51	6	12
Catholic Care North East	7	28	25
Information North (Northern Regional Library System)	4	1	2
Newcastle Community Law Centre	2	2	1
Disability North	16	6	2
Newcastle Family Service Unit	0	6	2
North East Innovation and Development Company Ltd.	11	5	4
Northern Regional Examinations Board	0	4	14
Northern Provincial Councils	8	2	4
Northern Arts Association	39	20	6
Northern Council for Further Education	2	16	12
Northern Counties School for the Deaf	38	13	16
North of England Assembly of Local Authorities	13	1	2

Northumbria Tourist Board	15	16	5
Park View Sports Complex	3	1	0
Port of Tyne Authority	0	0	4
Praxis Service	3	2	0
Search Project	3	0	1
Shiremoor Advice Centre	1	4	0
St. Mary Magdalene and Holy Jesus Charity	6	1	3
Sunderland Empire Theatre Trust Ltd.	9	3	5
Sunderland Enterprise Agency	0	0	0
Sunderland Outdoor Activities Association	0	3	0
The Ozanam House Probation Hostel Management Committee	15	3	2
Theatre Royal Trust Ltd.	44	3	14
Tyne and Wear Development Corporation	0	42	22
Tyne and Wear Enterprise Trust Ltd.	21	6	5
Tyne Theatre Trust (Northern Stage Company)	0	0	0
Tyne and Wear Development Company Ltd.	6	11	2
Tyneside Training and Enterprise Council	194	26	8
Wallsend Citizens' Advice Centre	3	0	0
Wallsend Peoples' Centre	4	0	0
Workshops for the Adult Blind (Palatine Products)	68	16	89
Sunderland City Training and Enterprise Council	120	21	3
South Tyneside Groundwork Trust	6	2	0
Sunderland Arts Centre	0	0	0
Tyne Waste Ltd.	0	19	4
Newcastle West End Partnership	0	2	0
North Tyneside City Challenge	5	3	0
Wellfield Middle School	2	0	0
Newcastle Youth Congress	1	1	0
Gateshead Law Centre	4	2	0
Newcastle Tenants Federation	6	1	0
Hebburn Neighbourhood Advice Centre	2	0	0
North Tyneside Child Care Enterprise Trust	12	8	0
Learning World	5	2	0
Norcare	2	0	0
National Glass Centre	0	1	0
North Tyneside Disability Advice Centre	0	0	1
Northern Informatics Application Agency	2	1	0
International Centre for Life Trust	20	0	0
Simonside Community Centre	1	0	0
Tyne and Wear Play Association	0	0	0
Benton Grange School	0	1	11
One North East	0	3	2
H.E.F.C.E.	0	2	8
Passenger Transport Company	0	0	92
The Hospital of St. Mary the Virgin	0	0	1
Sub Totals	1,592	595	955
GRAND TOTALS	41,043	9,879	25,245

INVESTMENT REPORT

ARRANGEMENTS

The Pensions Committee is required to make arrangements for the investment of the Fund. These arrangements have to comply with legal requirements, including the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998. These regulations set out the types of investments which can be made, which include company and government securities, property and unit trusts, and set out restrictions on the proportion of the Fund which can be held in certain types of investment.

Acting within the requirements of legislation, and having taken appropriate advice, the Committee has set investment objectives and an investment policy for the Fund. It has then set up an investment management structure which provides exposure to a suitably diversified, but complementary, range of investment styles and processes. Investment managers have been appointed to operate within this structure and responsibility for the selection of individual investments has been delegated to these managers.

OBJECTIVES

The formal investment objectives are to:

- maintain securely a portfolio of assets of appropriate liquidity which will generate income and capital growth which, together with employer and employee contributions, will meet the cost of current and future benefits which the Fund provides, as set out in the relevant statutory documentation
- and
- minimise the long term costs of the Fund by maximising the return on the assets, whilst having regard to the objective set out above.

POLICY

Having regard to the Fund's financial position, statutory status and liability profile, it is believed to be appropriate to focus on maximising the long term return from the assets. It is regarded as inappropriate to be overly concerned about shorter term fluctuations in the value of the assets.

Accordingly, it is considered that a diversified portfolio of U.K. and overseas stock market securities and property, with a strong bias towards "real" assets, currently represents a suitable strategic asset allocation benchmark for the Fund. The benchmark would typically be represented by the average, or consensus, asset allocation within the CAPS survey.

MANAGEMENT STRUCTURE

The investment management structure which was in place until 1998 divided the Fund into four portions - three large broadly equal portions and a fourth smaller portion. Two of the large portions had been allocated to balanced managers and the third was operated on a specialist basis with a consensus asset allocation. The U.K. equity content of the third portion was indexed against the FTSE-Actuaries All-Share Index and active specialist managers had been appointed to invest in the overseas equity markets and in global bonds.

The fourth smaller portion contained the Fund's property investments, which were the responsibility of a specialist manager.

In order to avoid taking a short term view of investment performance, pension fund returns are generally assessed over five year periods. The Fund's average annual return over the five years to 1998 was 14.0%, which was comfortably above the rate of inflation and the increase in wages over the period, but was below the median U.K. pension fund return for the period of 14.9%.

The monitoring of each manager's performance over the five year period indicated that the portion of the Fund which was under specialist management had performed satisfactorily, as had the property portfolio. However, the balanced mandates had underperformed their objective. Their asset allocation in the latter part of the period had been overly defensive at a time when financial markets had, in the main, performed strongly. Furthermore, stock selection had been

weak in certain areas. Because almost two thirds of the Fund was under balanced management during this period, this had adversely affected the Fund's overall performance.

The Committee undertook a detailed review of the Fund's investment management structure. This review commenced in March 1998 and was completed in November 1998. The outcome has been an adjustment to the structure to provide for broadly equal amounts of the Fund to be under balanced and specialist management. This has been achieved by increasing the amounts managed by the existing global bonds and overseas equity managers and by introducing a new manager, Morley Fund Management, to actively manage a U.K. equity portfolio.

A balanced mandate held by Mercury Asset Management has been terminated and a smaller mandate awarded to Fidelity Institutional Asset Management, whilst a balanced mandate held by Phillips and Drew has been slightly reduced in size.

These revised arrangements were in full operation by January 1999.

OBJECTIVES AND RESTRICTIONS

The Committee has set objectives and restrictions for the investment mandates. These have been prepared with the aims of ensuring a prudent approach to investment and of allowing each manager to implement their natural investment style and process.

In addition to the specific restrictions on each mandate, which are set out in the individual investment management agreements, all managers are required to comply with the requirements of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998.

The two balanced managers, Phillips and Drew and Fidelity, are required to maintain well diversified portfolios which cover all major asset classes with the exception of property. With regard to asset allocation, broad guidelines have been set within which they must invest. These guidelines are reviewed at regular intervals in the light of economic and stockmarket conditions, the future benefits liabilities of the Fund and the views of the Investment Advisor and managers.

The objective for each balanced manager is to produce a return over five year rolling periods which exceeds the CAPS median return (excluding property), with the return in any individual year not falling significantly below that benchmark.

The part of the Fund which is under specialist management has continued to be operated with a consensus asset allocation. As a result of the changes which took place in 1998, two thirds of the U.K. equity content of this "consensus portfolio" is indexed against the FTSE-Actuaries All-Share Index, whilst the remaining one third is managed actively. Active specialist managers continue to invest in the overseas equity markets and in global bonds.

The managers who have been appointed to this portfolio are:

Barclays Global Investors	-	Asset allocation and U.K. equity indexed portfolio
Morley Fund Management	-	U.K. equity active portfolio
Prudential Portfolio Managers	-	Global bonds
J.P. Morgan Investment Management	-	U.S. equities
Capital International	-	European equities
Schroder Investment Management	-	Far Eastern equities.

These managers have been set targets, based on an appropriate index, which require outperformance over three year rolling periods. An annual downside target has also been set.

The property portfolio has continued to be managed on an advisory basis by Argyll Property Asset Managers. Argyll is also responsible for advising the Committee on the proportion of the Fund's assets which should be invested in property.

CUSTODIANS

The Committee is prepared to appoint each manager's in-house or recommended custodian to act as custodian for each investment mandate, providing that criteria on security of assets and service standards can be met. Where a manager does not recommend a custodian, the Committee will make the appointment.

The custodians for the portfolios are:

Manager	Custodian
Phillips and Drew	UBS Asset Administration
Fidelity	RBS Trust Bank
Barclays Global Investors	Morgan Stanley Trust Company
Morley Fund Management	Citibank
Prudential Portfolio Managers	Boston Safe Deposit and Trust Company and Midland Bank
J.P.Morgan Investment Management	Bank of New York
Capital International	Bankers Trust Company
Schroder Investment Management	Schroder Investment Management.

CORPORATE GOVERNANCE AND VOTING

The Committee believes that good corporate governance and the informed use of voting rights are an integral part of the investment process which should improve the long term performance of the companies in which the Fund is invested. Voting rights are regarded as an asset which needs managing with the same duty of care as any other asset. The use of these rights is essential to protect the interests of the organisations participating in the Fund and the beneficiaries of the Fund.

It is essential that this process is carried out in an informed manner and, for this reason, the Committee believes that the Fund's investment managers are best placed to undertake it.

The Committee requires each manager to prepare a document which sets out their policy on corporate governance and on the use of voting rights.

This policy has to provide for:

- the approach towards U.K. quoted companies to take account of the recommendations of appropriate studies, in particular the strong guidance offered by the Cadbury and Greenbury Codes, the Hampel Report and the Combined Code produced by the Hampel Committee
- the approach towards companies outside the U.K. to take account of the practices of the home nation
- voting rights to be exercised in a manner which establishes a consistent approach to both routine and exceptional issues, in order that company directors fully understand the managers' views and intentions.

Whilst the Committee requires each manager to exercise voting rights in accordance with their individual policy, it retains the right to direct the manager in respect of any particular issue should such action be considered appropriate.

Each manager is required to:

- report any material change to their policy immediately
- provide an annual report which sets out their policy and the manner in which it has been implemented
- provide a quarterly report which sets out their voting record.

REPORT FOR 1998/99

Strategy

The Fund's balanced managers have discretion to implement their own asset allocation, subject to complying with broad guidelines, whilst the asset allocation within which the specialist managers operate is set in line with the consensus. The main combined effect of these strategies in 1998/99 was a movement out of U.K. index-linked and overseas equities and into U.K. fixed interest, overseas bonds and U.K. equities.

The allocation to property is set by the Pensions Committee, acting in the light of advice from the Actuary and the Property Manager. In 1998/99, the Committee determined that this allocation should be increased in order to keep it broadly in line with the average allocation to property of other large pension funds.

The actions of the investment managers and of the Pensions Committee had the following effect on the Fund's asset allocation:

	Start of Year	Movement During Year	End of Year
	£'m	£'m	£'m
U.K. fixed interest	158	42	200
U.K. Index-linked	66	-34	32
Overseas bonds	95	87	182
U.K. equities	944	33	977
Overseas equities	332	-38	294
Property	109	16	125
Net current assets	154	11	165
	<u>1,858</u>	<u>117</u>	<u>1,975</u>

Investment Returns

For the 1998/99 year, the Fund's return was 6.4%. This was 0.5% below the CAPS median pension fund return of 6.9%.

The table below analyses the Fund's total return over the main investment markets and compares it against the CAPS median and index returns:

	Tyne and Wear Fund	Median Fund	Index
	%	%	%
Total Fund	+6.4	+6.9	-
U.K. fixed interest	+16.9	+15.7	+14.3
U.K. index-linked	+19.7	+19.5	+18.5
Overseas bonds	+7.7	+10.8	+13.8
U.K. equities	+3.5	+5.0	+6.8
Overseas equities	+9.9	+8.6	+16.6
U.S.	+23.2	+22.4	+23.8
Japan	+22.3	+21.9	+19.5
Europe	+6.7	+6.8	+7.7
Pacific Basin	-2.9	-2.9	-1.2
Property	+12.1	+11.3	+10.9

The index returns indicate how markets performed during 1998/99. Returns were positive in all the areas referred to, with the exception of Pacific Basin equities.

The strongest returns came from U.S. equities. That market returned 23.8% in Sterling terms and reached a record high due to strong economic growth which, combined with a benign outlook for inflation, had led to low interest rates. The U.K. equity market also reached a record high, but then fell back as it responded to concerns over slow economic growth

and finally produced a more modest return of 6.8%. The return from European equities, which was 7.7%, was also held back by concerns over future growth. Japanese equities are shown to have returned 19.5%, but this was largely attributable to a recovery in value of the Yen, because the absence of a recovery in that economy meant that the return in local terms was only 2.4%. The economic crisis in Asia meant that the Pacific Basin markets continued to be volatile and produced a negative return of -1.2%.

The overall background of non inflationary economic growth was positive for the fixed interest asset classes. U.K. fixed interest returned 14.3%, whilst overseas bonds returned 13.8%. U.K. index-linked returned 18.5%.

The Tyne and Wear Fund outperformed the median pension fund for U.K. fixed interest, U.K index-linked, U.S. equities, Japanese equities and property. However, it underperformed in overseas bonds, European equities and in the important U.K. equities asset class.

Overall, the 0.5% underperformance of the Total Fund against the median return is attributable to stock selection.

Five Year Returns

The performance of the Fund is normally judged on the results of the latest five year period. In the individual years, the returns have been:

	Tyne and Wear Fund	Median Fund
	%	%
1994/95	+2.3	+0.6
1995/96	+20.9	+23.4
1996/97	+10.9	+11.1
1997/98	+21.7	+23.4
1998/99	+6.4	+6.9

These results have produced an average annual return over the five year period of 12.2%, which is 0.3% below the median return of 12.5%. However, it is comfortably above the rate of price and earnings inflation to which the Fund's liabilities are linked.

For this five year period, the underperformance against the median is attributable in part to stock selection. However, the investment strategies of the individual managers combined into a strategy for the Fund as a whole which has been relatively defensive. Because investment returns from most markets have been strong over the period, this defensive strategy, and in particular an underweight position in U.K. equities, has detracted from performance.

ACTUARIAL INFORMATION

Introduction

Legislation requires that an actuarial valuation is carried out every third year. The purpose of this is to establish that the Fund is able to meet its liabilities to past and present contributors.

The actuarial information set out below complies with the disclosure requirements of SSAP 24.

Actuarial Position

1. Rates of contribution paid by the participating employers during 1998/99 were based on the actuarial valuation carried out as at 31st March 1995.
2. This valuation showed that the required level of contributions to be paid to the Fund by the Metropolitan District Councils with effect from 1st April 1996 was as set out in the following schedule:

Metropolitan Borough Council	1 April 1996 to 31 March 1997		1 April 1997 to 31 March 1998		1 April 1998 to 31 March 1999	
	%	+ £'000	%	+ £'000	%	+ £'000
Gateshead	140	-	145	946	145	1,998
Newcastle	140	-	145	824	145	1,739
North Tyneside	135	-	140	508	140	1,076
South Tyneside	135	-	140	740	140	1,564
Sunderland	140	-	145	1,136	145	2,516

Percentages shown are percentages of members' contributions.

Monetary amounts shown are payable in addition to the percentages of members' contributions.

3. These rates of contribution are the rates which, in addition to the contributions paid by the members, are sufficient to meet:
 - 100% of the liabilities arising in respect of service after the valuation date plus
 - an adjustment over the members' average future service lifetime to reflect the shortfall of the value of each participating employer's notional share of the Fund's assets over 100% of its accrued liabilities, allowing, in the case of members in service, for future pay increases.

The large increase in rates found to be necessary is being phased in over a period of years.

4. The market value of the Fund's assets at the valuation date was £1,174 million and the actuarial value of £1,131 million represented 87.4% of the Fund's accrued liabilities, allowing for future pay increases.
5. The contribution rates have been calculated using the projected unit actuarial method and the main actuarial assumptions were as follows:

Rate of return on investments	8½% per annum
Rate of general pay increases	6% per annum
Rate of increases to pensions in payment (in excess of GMPs)	4% per annum
Valuation of assets	discounted value of future income, assuming that that part of the assets notionally reinvested in the FT All-Share Index will achieve 4% per annum dividend growth.

6. The abolition in the July 1997 Budget of the ability of pension funds to reclaim Advance Corporation Tax credits has reduced the immediate income from U.K. equities by 20% and the overall income to the Fund by around 10%. There were, however, some mitigating features, such as the reduction in Corporation Tax from 33% to 31% and the net effect may be to reduce yields on funds by about 1/3% per annum. This implies a reduction in the funding level of some 8%, together with an increase in the costs of accruing benefits of about 20% of employee contributions. In order to meet these, an increase in employers contributions of about 65% of employee contributions (3.7% of payroll) may be required.
7. An actuarial valuation was carried out as at 31st March 1998 and changes in the contribution rate as a result of that valuation became effective from 1st April 1999.

REPORT OF THE ACTUARY FOR THE YEAR ENDED 31ST MARCH 1999

1. The last full actuarial investigation into the financial position of the Tyne and Wear Pension Fund in accordance with Regulation 77(1) of the Local Government Pension Scheme Regulations 1997 was completed as at 31st March 1998. The results showed that the financial position of the Fund had deteriorated since the previous valuation with the assets covering 86.7% of the liabilities, allowing for future pay increases in pensionable remuneration.
2. We recommended revised rates of contributions to be paid by the participating employers with effect from 1st April 1999. A formal Certificate of these contribution rates to be paid from 1st April 1999 was issued to the Director of Corporate Services of the South Tyneside Metropolitan Borough Council as part of our formal report on the valuation of the Fund as at 31st March 1998.
3. Having regard to the results of the actuarial valuation as at 31st March 1998 and the rates of contribution in payment from 1st April 1999, together with the stepped increases recommended to apply in future years, the assets of the Fund as at 31st March 1999 will be sufficient, on the basis of the assumptions adopted for the valuation as at 31st March 1998, to meet the on-going liabilities of the Fund under the Regulations associated with both the accrued service and the currently accruing service, increasing levels of pensionable remuneration and increases to pensions both in payment and in deferment, taking into account the gradual amortisation of the deficiency disclosed by the valuation as at 31st March 1998.
4. The next actuarial valuation of the Pension Fund will be carried out as at 31st March 2001 and the results will be reported in the accounts for the year ending 31st March 2002.

R.G. Ashurst

**Fellow of the Institute of Actuaries
Watson Wyatt Partners**

Fund Account

1997/98		Note	1998/99	
£'000	£'000		£'000	£'000
Contributions and benefits				
79,132		3	87,673	
<u>8,647</u>		4	<u>14,248</u>	
	87,779			101,921
83,161		5	89,018	
6,323		6	6,355	
<u>1,335</u>		7	<u>1,292</u>	
	<u>90,819</u>			<u>96,665</u>
	-3,040			5,256
Net additions (withdrawals) from dealings with members				
Returns on investments				
66,520		8	72,786	
262,945		9	42,334	
<u>-2,654</u>		10	<u>-2,913</u>	
	<u>326,811</u>			<u>112,207</u>
	323,771			117,463
	<u>1,534,251</u>			<u>1,858,022</u>
	<u>1,858,022</u>			<u>1,975,485</u>

Net Assets Statement

1997/98		Note	1998/99	
£'000	£'000		£'000	£'000
Investments				
237,672		9		290,696
1,196,664				1,183,622
80,005				65,487
83,386				147,944
105,197				122,231
275				50
155,474				150,276
<u>-13,049</u>				<u>-361</u>
	1,845,624			1,959,945
	<u>12,398</u>			<u>15,540</u>
	<u>1,858,022</u>	11		<u>1,975,485</u>
Current assets and liabilities				
Net assets of the Fund at 31st March				

Notes to the Financial Statements

1. Basis of Preparation

The financial statements have been prepared in accordance with the main recommendations of the Statement of Recommended Practice, Financial Reports of Pension Schemes and follow the 1998 Code of Practice on Local Authority Accounting issued by the Chartered Institute of Public Finance and Accounting.

The figures for 1997/98 have been restated where appropriate to reflect the changes in accounting practices which arose from the introduction of the new SORP.

The financial statements summarise the transactions of the Fund and deal with the net assets at the disposal of the Council. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Fund year. The actuarial position of the Fund, which does take account of such obligations, is dealt with in statements prepared by the Actuary, which are on pages 18 and 19. The financial statements should be read in conjunction with the Actuary's statements.

2. Accounting Policies

Valuation of Investments

Quoted securities have been valued at their mid-market closing price on 31st March 1999.

Unitised securities have been included at the average of their bid and offer prices on 31st March 1999.

Other unquoted investments have been valued with regard to latest dealings and other appropriate financial information.

Overseas investments and foreign currency balances have been converted into Sterling at the closing exchange rates on 31st March 1999.

Properties are shown as valued at 31st December 1998 by chartered surveyors, with the exception of one property purchased after that date which has been valued at cost. The valuers are Fellows of the Royal Institute of Chartered Surveyors from Drivers Jonas, Jones Lang Le Salle and Richard Ellis.

Investment Transactions

Investment transactions which were not settled as at 31st March 1999 have been accrued.

Investment Income

Investment income has been credited to the Fund on the ex-dividend date and is grossed up to allow for recoverable and non-recoverable tax. Non-recoverable tax has been shown as an expense.

Foreign income received during the year has been converted into Sterling at the exchange rate at the date of transaction. Amounts outstanding at the year end have been valued at the closing exchange rates on 31st March 1999.

With regard to property rental income payable quarterly in advance, only the proportion of each payment attributable to the Fund from the due date to the 31st March 1999 is credited to the Fund Account.

Interest on cash deposits has been accrued up to 31st March 1999.

Investment Management Expenses

Investment management expenses payable as at 31st March 1999 have been accrued.

Debtors and Creditors

For Fund transactions, a system of income and converted payments is operated. Unless stated below, at the year end payments are converted to expenditure by the addition of unpaid creditors as at 31st March 1999. The accrual concept is in accord with SSAP 24.

Contributions

Contributions represent the amounts receivable from the organisations participating in the Fund; these may be district councils, other scheduled bodies or admitted bodies. Such amounts relate both to their own employer contributions and those of their pensionable employees. The rate for employers is determined by the Actuary. Contributions due as at 31st March 1999 have been accrued.

Benefits, Refunds and Transfer Values

Benefits and refunds are accounted for in the year in which they become due for payment. Transfer values are accounted for on a payments/receipts basis since not only do they frequently apply to several past years but, in the case of transfer values due, information is not available at the year end on which to make an accrual.

3. Contributions Receivable

	1998/99	1997/98
	£'000	£'000
Employers		
Normal	45,927	44,997
Additional	10,659	4,716
Members		
Normal	31,076	29,381
Additional voluntary contributions	11	38
	<u>87,673</u>	<u>79,132</u>

4. Transfers In

During the year, individual transfers in from other schemes amounted to £14.248 million (£8.647 million in 1997/98)

5. Benefits Payable

	1998/99	1997/98
	£'000	£'000
Pensions	80,312	71,315
Commutations and lump sum retirement benefits	15,871	16,377
Lump sum death benefits	1,370	1,134
Less: Recharges	-8,535	-5,665
	<u>89,018</u>	<u>83,161</u>

6. Payments To And On Account Of Leavers

	1998/99	1997/98
	£'000	£'000
Refunds to members leaving service	449	426
Individual transfers to other schemes	5,906	5,897
	<u>6,355</u>	<u>6,323</u>

7. Administration Expenses

The Local Government Pension Scheme Regulations 1997 permit costs incurred in connection with the administration of the Fund to be charged against the Fund. A breakdown of the costs is set out below.

	1998/99	1997/98
	£'000	£'000
Employee expenses	722	661
Support services recharge	561	610
Printing/publications	36	48
Actuarial fees	62	20
Other expenses	105	80
SIB pension review	-157	-52
Other income	-37	-32
	<u>1,292</u>	<u>1,335</u>

Employee expenses have been charged to the Fund on the basis of time spent on previous administration. Office expenses and other overheads have also been charged.

8. Investment Income

	1998/99	1997/98
	£'000	£'000
Fixed interest securities	16,754	15,648
Equities	34,565	38,591
Index-linked securities	2,075	2,118
Managed and unitised funds	3,544	2,710
Properties – net rents	9,394	5,699
Loans	11	15
Cash deposits	10,717	6,921
Underwriting commission	40	8
Sub-total	<u>77,100</u>	<u>71,710</u>
Less: Non-recoverable tax	-4,314	-5,190
Total investment income	<u>72,786</u>	<u>66,520</u>

9. Investments

	Value at	Purchase at	Sales	Change in	Value at
	1.4.98	Cost	Proceeds	Market	31.3.99
	£'000	£'000	£'000	Value	£'000
				£'000	
Fixed interest securities	237,672	394,400	-352,055	10,679	290,696
Equities	1,196,664	493,983	-527,222	20,197	1,183,622
Index-linked securities	80,005	41,464	-63,064	7,082	65,487
Managed and unitised funds	83,386	140,283	-76,599	874	147,944
Properties	105,197	19,049	-5,555	3,540	122,231
Loans	275	0	-225	0	50
	<u>1,703,199</u>	<u>1,089,179</u>	<u>-1,024,720</u>	<u>42,372</u>	<u>1,810,030</u>
Cash deposits	155,474	9,195	-14,406	13	150,276
Other investment balances	-13,049	-2,025	14,764	-51	-361
	<u>1,845,624</u>	<u>1,096,349</u>	<u>-1,024,362</u>	<u>42,334</u>	<u>1,959,945</u>

The changes in market value of investments during the year comprise all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

	1998/99	1997/98
	£'000	£'000
Fixed Interest Securities		
U.K. public sector	157,827	156,144
U.K. other	9,780	1,389
Overseas public sector	121,121	79,973
Overseas other	1,968	166
	<u>290,696</u>	<u>237,672</u>
Equities		
U.K. quoted	954,329	919,420
U.K. stock index futures	3,284	5,311
U.K. unquoted	380	559
Overseas quoted	225,616	271,361
Overseas unquoted	13	13
	<u>1,183,622</u>	<u>1,196,664</u>
Index-Linked Securities		
U.K. quoted	27,479	65,588
Overseas quoted	38,008	14,417
	<u>65,487</u>	<u>80,005</u>

TYNE AND WEAR PENSION FUND

Managed and Unitised Funds			
U.K. managed funds	- other	124,422	0
U.K. unit trusts	- property	2,913	3,064
	- other	19,219	79,646
Overseas unit trusts	- other	<u>1,390</u>	<u>676</u>
		<u>147,944</u>	<u>83,386</u>
Properties			
Freehold		107,611	85,765
Long leasehold		<u>14,620</u>	<u>19,432</u>
		<u>122,231</u>	<u>105,197</u>
Loans			
		<u>50</u>	<u>275</u>
Cash Deposits			
Sterling		146,183	136,988
Foreign currency		<u>4,093</u>	<u>18,486</u>
		<u>150,276</u>	<u>155,474</u>
Other Investment Balances			
Cash backing open stock index futures		-3,284	-5,311
Currency hedging		199	444
Debtors		12,693	6,220
Creditors		<u>-9,969</u>	<u>-14,402</u>
		<u>-361</u>	<u>-13,049</u>

10. Investment Management Expenses

	1998/99	1997/98
	£'000	£'000
Administration, management and custody	2,808	2,992
Performance measurement services	39	37
Other advisory fees	62	31
Audit fees	4	8
Refund of VAT	<u>0</u>	<u>-414</u>
	<u>2,913</u>	<u>2,654</u>

Administration includes employee expenses which have been charged to the Fund on the basis of time spent on investment. Office expenses and other overheads have been charged.

11. Current Assets And Liabilities

	1998/99	1997/98
	£'000	£'000
Contributions and recharges due	6,785	5,405
Inland Revenue	-1,686	-1,401
Other	975	-516
Dividend accruals	9,995	8,122
Recoverable taxation	483	574
Investment management expenses	-1,012	-200
Refund of VAT	<u>0</u>	<u>414</u>
	<u>15,540</u>	<u>12,398</u>

TYNE AND WEAR PENSION FUND
12. Additional Voluntary Contributions

The Fund offers two types of AVC arrangements.

Additional years of services may be purchased within the Local Government Pension Scheme, with the contributions being invested as a part of the Fund's assets.

In addition, the Pensions Committee has chosen Equitable Life Assurance Society for the investment of other AVCs specifically taken out by Fund members. The Equitable Life scheme is a money purchase scheme and offers funding under three options – deposit, with profits or managed. This scheme, which is operated independently of the Fund, was valued at £2.950m as at 30th March 1999 (£1.920m - 30th March 1998).

13. Analysis of Investments Over Fund Managers

The market values of investments in the hands of each manager were: -

As at 31st March 1998		As at 31st March 1999	
£'000	%	£'000	%
		Balanced Managers	
-	-	Fidelity Institutional Asset Management	305,278 16
555,529	30	Mercury Asset Management	- -
624,900	34	Phillips and Drew	596,941 31
		Specialist Managers	
104,878	6	Argyll Property Asset Managers	125,144 6
385,246	21	Barclays Global Investors	432,719 22
59,841	3	Capital International	100,551 5
12,674	1	JP Morgan Investment Management	19,342 1
-	-	Morley Fund Management	182,343 9
78,400	4	Prudential Portfolio Managers	162,398 8
23,424	1	Schroder Investment Management	34,718 2
<u>732</u>	<u>-</u>	Managed in-house	<u>511</u> <u>-</u>
<u>1,845,624</u>	<u>100</u>	<u>1,959,945</u>	<u>100</u>

14. Taxation
U.K. Tax

The Fund is an exempt approved fund and is not liable to income tax or capital gains tax.

With effect from 2nd July 1997, the Fund cannot reclaim the tax credit on U.K. dividends.

The Fund is not registered separately from the Council for VAT and therefore can recover its input tax.

All investment income in the accounts has been shown gross of U.K. income tax and the non-recoverable element has been shown as an expense.

Overseas Tax

The Fund is subject to withholding tax in certain overseas countries. In all such cases, the investment income has been grossed up and non-recoverable tax has been shown as an expense.

15. Derivatives

A number of derivative instruments have been used by the Fund.

The Fund has used FT-SE 100 Index Futures to implement changes in asset allocation. As at 31st March 1999, the Fund held 52 June 1999 contracts which, when valued on the basis of associated economic exposure, had a book value of £3,299,037 and a market value of £3,283,800. The net variation margin paid to 31st March 1999 was therefore £15,237. The position was unwound by 16th June 1999 at an overall profit of £47,247.

The Fund has used forward currency contracts to hedge the currency exposure on overseas investments. As at 31st March 1999, the Fund held a range of positions which together showed an unrealised profit of £198,833. The positions showed an overall profit of £1,793,993 when unwound.

16. Underwriting

The Fund accepts a number of underwriting and placing propositions. As at 31st March 1999, no commitments were outstanding.

17. Contingent Liability - Tax Credit On Share Buybacks

Between 1994 and 1996, share buybacks were made by a significant number of major companies. Gross investors, including pension funds, received additional gains because an element of the buyback consideration could often be treated as a distribution of income rather than a return of capital and gross investors were, therefore, able to recover the tax credit involved.

The Inland Revenue's Compliance Division is seeking to establish the position under anti tax avoidance legislation. For this Fund, this could have the effect of denying recovery on tax credits totalling £2.8 million.

The technical considerations attaching to the anti avoidance legislation are complex and the position on recovery is unclear. Accordingly, any charge to the accounts will be taken in the year in which the position is clarified or is reasonably certain.

18. Cash Imbalance

In the 1997/98 South Tyneside MBC Statement of Accounts there was a contingent liability in respect of a cash imbalance between the banking and financial records. At that time, it was not known if the discrepancies related to the Council and/or the Pension Fund.

Further investigations have taken place during 1998/99 and discussions have been held with the external auditor. Amounts have been taken to revenue in the year to both the Council General Fund and the Tyne and Wear Pension Fund in order to clear this imbalance.

19. Audit

The accounts are presented subject to audit.

**TYNE & WEAR
PENSION FUND**

**Report & Accounts
1998/99**



**Administered by
SOUTH TYNESIDE METROPOLITAN BOROUGH COUNCIL**