



## **Pension Fund Sub-Committee**

14<sup>th</sup> February 2017

### **Report from the Chief Finance Officer**

For Information

Wards Affected:  
ALL

### **Investment Strategy and Asset Allocation**

#### **1.0 SUMMARY**

- 1.1 This report notes the Council's approved asset allocation strategy and investment overview, particularly in relation to the London Collective Investment Vehicle (CIV).

#### **2.0 RECOMMENDATIONS**

- 2.1 Members are asked to note the report.

#### **3.0 DETAIL**

- 3.1 The Pension Fund approved its strategic allocation in November 2015. Since then, it has been disinvesting in asset classes that do not meet that strategic allocation and re-allocating to assets that do.
- 3.2 The Pension Fund has exited all but £6m out of Property and has invested £6m into Infrastructure. It has no allocation towards Property and currently an 8% allocation towards Infrastructure. It has a £11.5m gap before it hits the allocation target. However, it is likely that we will over-allocate temporarily into Alinda Infrastructure III, as there are £20m of capital commitments. The Capital Dynamics Infrastructure element is more mature and it is anticipated that it will become more of a cash contributing asset than element of growth to the Fund.
- 3.3 The Private Equity Element is broadly on track to reduce to the intended 10% level. YFM represents the last few elements of a Fund that are being kept to maximise value. Capital Dynamics is also maturing and throwing off large amounts of cash naturally. In the next couple of years, subject to developments within the London CIV, the Pension Fund will need to consider re-allocating cash to it so that it maintains its allocation. It is not a priority according to the current asset allocation.

- 3.4 Fixed Income is under allocated at present. The fixed bond fund from Henderson only contains 11.6% of the 15% allocation but under the original investment strategy, multi-assets and other fixed income products were considered more appropriate investments, particularly in light of the risks of a bond market that many view as significantly over-priced. Henderson has also substantially under-performed the benchmark. It is being reviewed, as to how it protects itself against the potential down-turn in the market.
- 3.5 Diversified Growth Funds (DGFs) are at 9.5% of the 21% allocation. It is recommended to only add 6.5% or £50m of the Fund to another DGF until an internal review has identified as to whether the Triennial Review and the shift in the economic landscape might warrant an updated asset allocation. It is considered unlikely, all things being equal, that the asset allocation would move below 16%, if a new asset allocation was chosen, and therefore it should be safe to invest this amount. The split between the two DGFs is uncertain, as more detailed analysis needs to be undertaken, in the light of any investment decisions, therefore the figures in the table below are simply illustrative of the increase required to achieve the target.
- 3.6 Equity is divided into global and UK equity components. Together they equal 45%. It is broadly on a 2:1 allocation, respectively. Currently, it sits at 49.5% with the bulk of that in passive equity. The over-allocation stems from exiting Dimensional and prudently putting the difference into cheap tracker funds that performed very well over the past year (29.45% in L&G –World). However, this level of performance has led to the Pension Fund running up against the LGPS regulation of 35% under one mandate with the provider. The Pension Fund may choose to cut its global passive equity to keep below 35% but it would rather use up cash in the short-term as cash returns very little. The Fund will have greater latitude when it approves the new Investment Strategy Statement and tracker funds with their low costs are generally reviewed positively.
- 3.7 The increase to 5% of small cap equity was previously anticipated, so the Fund is simply delivering on its existing target allocation. However, that will temporarily increase its allocation to equity further. However, it is anticipated that once fixed income becomes available through the London CIV that the allocation would substantially reduce. Also, the passive equity will be replaced by active global equity managers under the current investment allocation. More details will follow from the London CIV presentation.
- 3.8 Cash currently comprises 11.1% of the Fund and without further investments, it would have grown due to Aviva proceeds and cash releases from Capital Dynamics exceeding the likely capital calls. The Fund would wish to keep a larger amount of cash on-hand than is normal, due to the need to re-allocate to other investments but it is still likely to end the year with cash at larger than it would have preferred (2.5-4%). It will make use of the Treasury to obtain investment returns greater than zero and protect the principal.
- 3.9 The asset allocation was developed in a significantly different economic environment to which the Pension Fund now finds itself. Furthermore, the actuarial results of the Triennial Review needs to be digested. Therefore, while

the Fund awaits decisions on the investment managers available through the London CIV, it will review as to whether the Asset allocation needs updating or refining. This will not delay actions already in train to exit asset classes or investments or future investment opportunities as the research cannot take place until cost-effective managers through the London CIV become available. However, it will make decisions about fixed income more challenging. Relative weightings between DGFs can also be reviewed during this period.

## Current Asset Allocation Strategy

Asset Class	Fund	Current		Allocation		Proposed	Variance	Solution
		£'000s	%	£'000s	%	£'000s	£'000s	
Equity	L&G - UK	102,507	13.19%	77,698	10.00%		(24,810)	Henderson small cap will hit target but Passive Equity will remain overweight till appropriate investments through the CIV become available.
Equity	L&G - World	253,643	32.64%	155,395	20.00%		(98,248)	
Equity	Global Active	0		77,698	10.00%		77,698	
Equity	Henderson – small cap	28,069	3.61%	38,849	5.00%	10,780	0	
<b>Equity Total</b>		<b>384,219</b>	<b>49.45%</b>	<b>349,639</b>	<b>45.00%</b>	<b>10,780</b>	<b>(45,360)</b>	
DGF	Baillie Gifford	73,820	9.50%	73,820	9.50%		0	Taking time to ensure investment allocation is correct but on track.
DGF	2 <sup>nd</sup> DGF	0	0.00%	89,345	11.50%	50,000	39,345	
<b>Diversified Growth Fund Total</b>		<b>73,820</b>	<b>9.50%</b>	<b>163,165</b>	<b>21.00%</b>	<b>50,000</b>	<b>39,345</b>	
Fixed Income	Henderson Multi-Asset	89,886	11.57%	0	0.00%		(89,886)	Staying in Henderson for the moment. However, under active review due to risks within bond market.
Fixed Income	Credit?	0		116,546	15.00%		116,546	
<b>Fixed Income Total</b>		<b>89,886</b>	<b>11.57%</b>	<b>116,546</b>	<b>15.00%</b>	<b>0</b>	<b>26,660</b>	
Infrastructure	Alinda Capital	40,564	5.22%	62,158	8.00%		21,594	Slowly growing as and when Capital Calls are actioned. No action required.
Infrastructure	Dynamics	11,532	1.48%	0	0.00%		(11,532)	
<b>Infrastructure Total</b>		<b>52,096</b>	<b>6.70%</b>	<b>62,158</b>	<b>8.00%</b>	<b>0</b>	<b>10,062</b>	
Private Equity	Capital Dynamics	84,109	10.83%	77,698	10.00%		(6,412)	Will drift down automatically. No action required.
Private Equity	YFM Equity Partners	585	0.08%	0	0.00%		(585)	
<b>Private Equity Total</b>		<b>84,694</b>	<b>10.90%</b>	<b>77,698</b>	<b>10.00%</b>	<b>0</b>	<b>(6,997)</b>	
Property	Aviva UK	2,224	0.29%	0	0.00%		(2,224)	Exiting property market gradually. No action required.
Property	Aviva Europe	3,622	0.47%	0	0.00%		(3,622)	
<b>Property Total</b>		<b>5,846</b>	<b>0.75%</b>	<b>0</b>	<b>0.00%</b>	<b>0</b>	<b>(5,846)</b>	
<b>Cash</b>		<b>86,414</b>	<b>11.12%</b>	<b>7,770</b>	<b>1.00%</b>	<b>(60,780)</b>	<b>(17,865)</b>	Cash will be needed to fund re-allocation.
<b>GRAND TOTAL</b>		<b>776,975</b>	<b>100.00%</b>	<b>776,975</b>	<b>100.00%</b>	<b>0</b>	<b>0</b>	

## 4.0 FINANCIAL IMPLICATIONS

- 4.1 These are no direct financial implications of this report. However, it is important that having the correct investment allocation, as arguable this has the biggest impact on fund performance. The timing of accessing cost effective investment managers that fit the Fund's asset allocation is inevitably both an enabling factor in the Fund performance and also an obstacle, when there are delays.

## 5.0 DIVERSITY IMPLICATIONS

- 5.1 None.

## 6.0 STAFFING IMPLICATIONS

- 6.1 None.

## **7.0 LEGAL IMPLICATIONS**

7.1 None.

## **8.0 BACKGROUND INFORMATION**

8.1 Henderson Investors – December 2016 quarterly report  
Legal & General – December 2016 quarterly report  
Northern Trust Performance Report December 2016

## **9.0 CONTACT OFFICERS**

9.1 Persons wishing to discuss the above should contact Gareth Robinson in the Investment and Pensions Section, on 020 8937 6567 at Brent Civic Centre.

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