

Pension Committee Agenda



To: Councillor Andrew Pelling (Chair)
Councillor Simon Hall (Vice-Chair)
Councillors Patricia Hay-Justice, Clive Fraser, Robert Canning,
Luke Clancy, Simon Brew, Yvette Hopley, Gill Driver and Peter Howard

Reserve Members: Maddie Henson, Jamie Audsley, Sherwan Chowdhury,
Steve Hollands, Robert Ward and Stuart Millson

A meeting of the **Pension Committee** which you are hereby summoned to attend,
will be held on **Tuesday, 4 December 2018 at 10.00 am** in **Council Chamber -
Town Hall**

JACQUELINE HARRIS BAKER
Director of Law and Governance
London Borough of Croydon
Bernard Weatherill House
8 Mint Walk, Croydon CR0 1EA

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www.croydon.gov.uk/meetings
Monday, 26 November 2018

Members of the public are welcome to attend this meeting.
If you require any assistance, please contact the person detailed above, on the
righthand side.

N.B This meeting will be paperless. The agenda can be accessed online at
www.croydon.gov.uk/meetings

AGENDA – PART A

1. Apologies for Absence

To receive any apologies for absence from any members of the Committee.

2. Minutes of the Previous Meeting (Pages 5 - 6)

To approve the minutes of the meeting held on 21 November 2018 as an accurate record.

3. Disclosure of Interests

In accordance with the Council's Code of Conduct and the statutory provisions of the Localism Act, Members and co-opted Members of the Council are reminded that it is a requirement to register disclosable pecuniary interests (DPIs) and gifts and hospitality to the value of which exceeds £50 or multiple gifts and/or instances of hospitality with a cumulative value of £50 or more when received from a single donor within a rolling twelve month period. In addition, Members and co-opted Members are reminded that unless their disclosable pecuniary interest is registered on the register of interests or is the subject of a pending notification to the Monitoring Officer, they are required to disclose those disclosable pecuniary interests at the meeting. This should be done by completing the Disclosure of Interest form and handing it to the Democratic Services representative at the start of the meeting. The Chair will then invite Members to make their disclosure orally at the commencement of Agenda item 3. Completed disclosure forms will be provided to the Monitoring Officer for inclusion on the Register of Members' Interests.

4. Urgent Business (if any)

To receive notice of any business not on the agenda which in the opinion of the Chair, by reason of special circumstances, be considered as a matter of urgency.

5. Forward Plan (Pages 7 - 10)

6. Update on Asset Allocation (Pages 11 - 14)

7. Transition to Emerging Markets Fund (Pages 15 - 20)

**8. Progress Report for Quarter Ended 30 September 2018 (Part A)
(Pages 21 - 28)**

9. Exclusion of the Press and Public

The following motion is to be moved and seconded where it is proposed to exclude the press and public from the remainder of a meeting:

“That, under Section 100A(4) of the Local Government Act, 1972, the

press and public be excluded from the meeting for the following items of business on the grounds that it involves the likely disclosure of exempt information falling within those paragraphs indicated in Part 1 of Schedule 12A of the Local Government Act 1972, as amended.”

PART B

- 10. Minutes of the previous meeting (Part B) (Pages 29 - 30)**
To approve the minutes (Part B) of the meeting held on 21 November 2018 as an accurate record.

- 11. Progress Report for Quarter Ended 30 September 2018 (Part B)**
(Pages 31 - 50)

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Pension Committee

Meeting of the Pension Committee held on Wednesday, 21 November 2018 at 10.00 am in Council Chamber - Town Hall

MINUTES

Present: Councillor Andrew Pelling (Chair);
Councillor Simon Hall (Vice-Chair);
Councillors Patricia Hay-Justice, Clive Fraser, Robert Canning, Luke Clancy, Simon Brew and Yvette Hopley

Also Present: Co-opted Members (pensioner representatives) Gilli Driver and Peter Howard
Jonathan Bunt, Croydon Council
Nigel Cook, Head of Pensions and Treasury, Croydon Council
Michael Ellsmore, Chair of the Pension Board
Peter Gent, Senior Investment Consultant, Mercer
Sandra Herbert, Head of Corporate Law, Croydon Council
Richard Simpson, Director of Resources (Section 151 Officer), Croydon Council
Lisa Taylor, Director of Finance, Investment and Risk (Deputy S151 Officer), Croydon Council
Richard Warden, Scheme Actuary, Hymans
Robert McInvoy, Scheme Actuary, Hymans
Gary Delderfield, Partner, Eversheds

PART A

1/18 **Minutes of the Previous Meeting**

The minutes of the meeting held on 18 September 2018 were agreed as an accurate subject as amended to ensure that the Pension Board is correctly titled.

Matters arising: it was agreed that from the next meeting (4 December 2018), the Pension Committee will be webcast.

2/18 **Disclosure of Interests**

None.

3/18 **Urgent Business (if any)**

There were no items of urgent business.

4/18 **London Borough of Croydon Pension Fund Property Transfer Proposal**

The Committee **RESOLVED**:

- To receive into the Pension Fund, the 346 housing properties as set out in paragraph 3.1 of the report, from Croydon Council, between November 2057 and April 2059;
- To adjust Croydon Council's employer contribution rates to take account of the future transfer of properties. This will be based on assumed growth of CPI + 1.7% in the properties, which would result in a reduction of approximately 2.5% in the council's employer deficit contributions. This would be reviewed and adjusted if required in the triannual valuation; and
- To delegate to the Council's s151 Officer, in consultation with the Chair of the Pension Committee, to agree the appropriate wording of the Council resolution, to gain agreement of Full Council to transfer these assets from the Council's General Fund to the Pension Fund in 40 years.

Councillor Brew, Councillor Clancy, Councillor Hopley and Gilli Driver asked that their votes against the recommendations be noted.

5/18 **Exclusion of the Press and Public**

The following motion was **AGREED**:

"That, under Section 100A(4) of the Local Government Act, 1972, the press and public be excluded from the meeting for the following items of business on the grounds that it involves the likely disclosure of exempt information falling within those paragraphs indicated in Part 1 of Schedule 12A of the Local Government Act 1972, as amended."

A motion to sit in public was **AGREED** to allow the recommendations in 4/18 to be taken and debated in public.

Subsequently, the following motion was **AGREED** to allow for consideration of the Part B minutes of the meeting held on 18 September:

"That, under Section 100A(4) of the Local Government Act, 1972, the press and public be excluded from the meeting for the following items of business on the grounds that it involves the likely disclosure of exempt information falling within those paragraphs indicated in Part 1 of Schedule 12A of the Local Government Act 1972, as amended."

6/18 **Minutes of the previous meeting (Part B)**

The Part B minutes from the meeting held on 18 September 2018 were agreed as an accurate record.

7/18 **London Borough of Croydon Pension Fund Property Transfer Proposal
(Part B)**

Comments made by Cllr Clancy were noted.

The meeting ended at 12.35 pm

Signed:

Date:

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Croydon Council

REPORT TO:	Pension Committee 4 December 2018
SUBJECT:	Forward Plan
LEAD OFFICER:	Nigel Cook Head of Pensions and Treasury
CABINET MEMBER	Councillor Simon Hall Cabinet Member for Finance and Resources
WARDS:	All
CORPORATE PRIORITY/POLICY CONTEXT:	
Sound Financial Management: Ensuring that the pension fund is being given appropriate guidance and direction through the governance of the Pension Committee.	
FINANCIAL SUMMARY:	
There are no direct financial consequences to this report. However the implications of decisions taken by this Committee can be significant for the Revenue Account of the Council.	

1. RECOMMENDATIONS

- 1.1 That the Committee note the business plan for the coming year.

2. EXECUTIVE SUMMARY

- 2.1 It is recommended best practice for the Pension Committee (the Committee) to regularly review the forward plan. This report proposes a revised 2018/2019 forward plan which forms a business plan for the Committee.

3. DETAIL

- 3.1 The forward plan below sets out an agenda for each quarterly meeting to be held in the remainder of 2018/2019; however, further items may be added as required by senior officers in consultation with the Chair. As previously noted by the Committee in June 2018, there may be a need to add items in response to changing circumstances, such as any issues thrown up by the government's decision to require funds to pool assets, changes to the investment regulations or if there are further global market events requiring actions from the Committee.

- 3.2 The Committee has committed to a programme of training and in part, this can be delivered by sessions following on from or preceding the business part of the PEN 04122018

meeting. The content of training will be informed by the direction of future legislation; and the choice of investment vehicles.

3.3 The Local Pensions Board supports the Scheme Administrator (the Executive Director of Resources) and hence the Pensions Committee by considering a number of issues.. These are expected to include:

- Review of strategy and policy documents such as the Funding Strategy Statement and Investment Strategy Statement;
- Key Performance Indicators;
- Engagement with stakeholders;
- ESG (Ethical, Social and Governance) and voting matters;
- Assessment of the performance of professional advisors;
- Consideration of Myners principles;
- Matters relating to fees

3.4 Further the Board could review the following key policy documents, alerting the Committee to any matters that require their closer attention. These policies include, but are not limited to:

- Discretion's policy for the Council;
- Training policy for the Committee, Board and officers;
- Cessation Policy;
- Communications Policy;
- Terms of Reference for the Committee;
- Policy for Employers leaving the Fund;
- Internal Disputes Resolution Policy;
- Breaches of the Law policy;
- Administration Strategy;
- Conflicts of Interest Policy (for the Pensions Board); and
- Local Pension Board Annual Review.

3.5 Matters relating to admission agreements, schools converting to academies and other scheme employers will be reported to the Committee on an ad hoc basis.

3.6 **The Pension Committee 2019 – 2020 Business Plan**

Note that dates for 2019 are yet to be confirmed and will be circulated at a later date.

3.6.1 **12 March 2019**

- Progress report quarter ending December 2018 performance
- Risk Register review
- Forward Plan review
- Adopt revised Investment Strategy Statement
- Report back from Pensions Board
- KPIs
- Triennial Actuarial Valuation

3.6.2 June 2019

- Progress report quarter ending March 2019 performance
- Governance annual review
- Report back from Pensions Board

3.6.3 September 2019

- Progress report quarter ending June 2019 performance
- KPIs
- Review of Forward Plan
- Draft Annual Report
- External Auditors Report
- Local Pension Board Annual Report
- Review of Risk Register
- Investment Strategy Statement, consider revisions, including
- Review London CIV against Investment Strategy Statement (ISS) guidance (regulation (7) (2) d)
- Review of ESG investment principles for inclusion in ISS

3.6.4 December 2019

- Progress report quarter ending September 2019 performance
- Report back from Pensions Board

3.6.5 March 2020

- Progress report quarter ending December 2019 performance
- KPIs
- Report back from Pensions Board •
- Risk Register review
- Forward Plan review

3.8 This forward plan forms the business plan for the Committee. The Committee are asked to consider any changes necessary to the forward plan and subject to these, agree its adoption.

4 FINANCIAL CONSIDERATIONS

4.1 There are no further financial considerations flowing from this report.

5 OTHER CONSIDERATIONS

5.1 Other than the considerations referred to above, there are no customer Focus, Equalities, Environment and Design, Crime and Disorder or Human Rights considerations arising from this report

6 COMMENTS OF THE SOLICITOR TO THE COUNCIL

6.1 There are no additional legal implications arising from the recommendations within this report.

Approved by: Sandra Herbert, Head of Litigation and Corporate Law, for and on behalf of Jacqueline Harris-Baker, Director of Law and Governance and Monitoring Officer.

CONTACT OFFICER:

Nigel Cook, Head of Pensions Investment and Treasury,
Resources department, ext. 62552.

BACKGROUND DOCUMENTS:

Croydon Council

REPORT TO:	PENSION COMMITTEE 4 December 2018
SUBJECT:	Update on Asset Allocation Implementation
LEAD OFFICER:	Richard Simpson, Executive Director of Resources
CABINET MEMBER	Councillor Simon Hall Cabinet Member for Finance and Resources
WARDS:	All
CORPORATE PRIORITY/POLICY CONTEXT:	
<p>Sound Financial Management: Reviewing and ensuring that the performance of the Council's Pension Fund investments is in line with their benchmark and within the assumptions made by the Actuary.</p>	
FINANCIAL SUMMARY:	
<p>This report discusses the allocation of assets comprising the Pension Fund to different asset classes.</p>	

1	RECOMMENDATIONS
1.1	The Committee are asked to consider and note the contents of this report.

1 EXECUTIVE SUMMARY

- 1.1 This report summarises the current balance of allocations compared to the target asset allocation for the Pension Fund. In particular it describes the implications of the underweight position on the Private Rental Sector fund; the treatment of the gift of affordable housing properties; and the imbalance between equities and fixed interest and the actions being taken to address this.

2 Background

- 2.1 The September meeting of this Committee considered a paper drafted by Mercer, the Fund's investment advisors, which considered the structure of the Fund's current fixed income portfolio and the suitability of options currently available with the London CIV ("London CIV") and in the pipeline to be added to the LCIV in future. Although there are no directly comparable sub-funds in the London CIV, Mercer consider the PIMCO global credit fund to be the closest comparable option.

- 2.2 On this basis the Committee agreed to invest, over a period of time, the proportion of the portfolio allocated to fixed interest, less the current allocation to the Aberdeen Standard Life Absolute Return, to the London CIV PIMCO sub-fund.

Detail

- 2.3 Underpinning this process of optimising investment decisions, the asset allocation strategy determines the proportion of assets that the Fund has invested in. The mix of asset classes has been chosen because it should offer the greatest opportunity of achieving, over the long run, the target return of CPI + 2.2%, within a risk budget acceptable to the Committee. The strategy intends that assets are diversified, by asset classes, by investment philosophy and by region and currency. It is anticipated that different classes will perform differently in different macro-economic environments, noting that in the beginning of the Great Financial Crisis all assets behaved in a similar fashion.
- 2.4 The current strategy comprises five asset classes: equities; fixed interest; and alternatives – infrastructure, private equity, and property (commercial and residential). Cash is held for business reasons, not as an investment. Although each asset class, and indeed sub-category, is held because they demonstrate different characteristics, broad, high level features are relevant. Equity, under the present global conditions, is generating returns above expectations. It is also held because it is a very liquid asset, which is an attractive characteristic in the current climate where cash may be needed for rebalancing and is required to make up contribution shortfalls. In the medium to long-term there will be greater emphasis on this latter characteristic. Fixed interest funds are useful to match some of the liabilities of the Fund although there are other assets that could perform this function as they have an inflation index embedded. Certain infrastructure could be said to display this but with a higher level of risk, (and hence return).
- 2.5 Alternate assets are held to generate higher returns, access markets and investment opportunities not readily accessible through the listed markets, and ad hoc business opportunities. Most of the allocated risk budget for the overall portfolio is spent on these assets. This Croydon Fund, proportionately, has a greater exposure to alternate assets than the majority of UK LGPS Funds.
- 2.6 A long-term plan has been agreed by the Committee to allocate Pension Fund cash to these assets. Identifying asset managers, evaluating them, performing due diligence and making the investments can be a lengthy process. This has been further complicated by the development of the London CIV and the pooling agenda.
- 2.7 The current allocation to asset classes is in line with the long-term strategy. However there are two positions that need to be resolved. Due to lack of opportunities and a lengthy queue of investors, the allocation to residential property, through the M&G Private Rental Sector fund remains underweight (4% invested against a target of 6%). As the Croydon Fund will be evaluated as part of the Triennial Actuarial valuation, this might be an opportunity to revisit this allocation decision. The review of the asset allocation strategy will inform the Funding Strategy Statement.
- 2.8 The Private Rental Sector is developing and can be considered an innovative asset class. However a degree of expertise from the fund management team is necessary to ensure the best chance of achieving target returns. In turn this means that there

is a competition to acquire underlying assets and funds limit access to avoid diluting their offerings. As a consequence for this Fund, the strategic allocation has been only partially filled. The Committee should consider whether the current target allocation is appropriate, weighing up the opportunity cost of waiting for investment opportunities in a dynamic environment. This consideration should sit within the wider context of reviewing the asset allocation strategic as part of the triennial Actuarial Valuation.

2.9 At a special meeting of the Pensions Committee (21 November) it was decided to take forward a proposal to gift housing stock acquired for Croydon Affordable Housing LLP to the Fund at a future date in 40 years. The Committee should note that this asset category is distinct from the Private Rental Sector class discussed above. These houses have been acquired to meet a social need for decent, affordable housing. Private Rental Sector properties are acquired to generate a profit through rental income. They are directed at an entirely different housing needs. They will demonstrate different and distinct characteristics over the spread of economic environments the Fund could be expected to encounter. Furthermore, the current asset allocation strategy will not feature an allocation to social housing because this gifting process will not take place in the short-term, so that the strategy would be under-weight to social housing, should that be included, for the long-term, distorting the underpinnings of the Fund. The Funding Strategy will nevertheless include narrative to include this proposal as it will impact on the long-term development of the Fund.

2.10 The Committee has discussed the extent to which the imbalance between equities and Fixed Interest should be addressed and how. The decision has been taken to transfer a sum equivalent to the overweight position to the Global Fixed Interest sub-fund offered by the London CIV. This is considered the closest match available through the CIV. The existing investments with Aberdeen Standard Life and Wellington will also be transitioned to the CIV.

2.11 Based on current valuations this adjustment will look like this:

Disinvest from LGIM Equity fund	£ 80 m
from Aberdeen Standard Life	£ 62 m
from Wellington	£ 63 m
Which sums to	£ 205 m

Transfer to London CIV global bonds £ 205 m.

These figures assume that the bond market will continue to benefit from market uncertainty. The Aberdeen Standard Life Absolute Return fund will not be included in this process.

2.12 The London CIV Global Bonds sub fund is managed by PIMCO. The Croydon Fund is a seed funder of this investment together with Bexley. The seed funding is £100m. Due to the timetabling of dealing dates the initial Croydon investment is of £14 million. This will be followed by another £ 66 million from the LGIM, then the other two funds in turn.

3 CONSULTATION

3.1 Officers have fully consulted with the Pension Fund's advisers in preparing this report.

4 FINANCIAL CONSIDERATIONS

4.1 This report deals exclusively with the structure of the Council's Pension Fund.

5 COMMENTS OF THE COUNCIL SOLICITOR AND MONITORING OFFICER

5.1 There are no additional legal implications arising from the recommendations within this report.

Approved by: Sandra Herbert, Head of Litigation and Corporate Law, for and on behalf of Jacqueline Harris-Baker, Director of Law and Governance and Monitoring Officer.

6 OTHER CONSIDERATIONS

6.1 There are no Human Resource, Customer Focus, Equalities, Environment and Design, Crime and Disorder or Human Rights considerations arising from this report.

7 FREEDOM OF INFORMATION/DATA PROTECTION CONSIDERATIONS

7.1 This report contains confidential information which could be of a sensitive nature, disclosure of which could prejudice the commercial interest of the companies involved and those of the Council's Pension Fund.

CONTACT OFFICER:

Nigel Cook – Head of Pensions and Treasury
Corporate Resources Department, ext. 62552.

BACKGROUND DOCUMENTS:

None

Croydon Council

REPORT TO:	PENSION COMMITTEE 4 December 2018
SUBJECT:	Transition to Emerging Markets Fund
LEAD OFFICER:	Richard Simpson, Executive Director of Resources
CABINET MEMBER	Councillor Simon Hall Cabinet Member for Finance and Resources
WARDS:	All
CORPORATE PRIORITY/POLICY CONTEXT:	
Sound Financial Management: Reviewing and ensuring that the performance of the Council's Pension Fund investments is in line with their benchmark and within the assumptions made by the Actuary.	
FINANCIAL SUMMARY:	
This report details the transition of assets into the London CIV Emerging Markets sub-fund.	

1	RECOMMENDATIONS
1.1	The Committee are asked to note the contents of this report.

1 EXECUTIVE SUMMARY

- 1.1 This report summarises the cost implications of transitioning £55 million from the LGIM equity fund into the London CIV.

2 Background

- 2.1 The Pensions Committee took a decision to invest part of the allocation to global equities (£55 million) into an Emerging Market Fund. After some discussion it was decided to invest this sum in a sub-fund within the London CIV managed by Janus Henderson.

Detail

- 2.2 In order to ensure the integrity of this transaction and measure the costs involved, Analytics, a consultancy specialising in transition oversight, were retained to ensure that the Council's objectives were being met and the sum involved was protected during the transition. They have drafted a note, appended to this report as Appendix A, summarising the costs relating to this exercise.
- 2.3 In summary, there are three components to the costs associated with this exercise: costs relating to LGIM, managers of the donor fund; opportunity costs arising from being out of the market; and costs relating to the receiving fund. These are summarised here:

Table 1 Costs of Transition

Custody Charges	£ 3,552.00
LGIM Fund Spreads	£ 32,865.41
Anti-Dilution Levy	£ 191,828.58
Total	£228,245.99

- 2.4 Custody costs arise from switching stock out of the Developed World ex. Tobacco Fund for units in the main index funds. This strategy was adopted because these larger index funds are considerably more liquid and see more cash inflows. This helped reduce transaction costs and increased the chance of crossing the outflow with another investor's inflow to reduce spread, which would not be possible in the smaller fund.
- 2.5 The second item in the table refers to the spreads paid for redeeming from the LGIM funds. The third item is the 35 basis point anti-dilution levy paid on the two investments into the LCIV fund.
- 2.6 The LGIM costs came in lower than the initial fee estimate. The dilution levy is as expected at 35 basis points.
- 2.7 Over the period of the transition the Fund was out of market for the second injection (of £27.5 million) between 2nd and 5th November. The emerging markets fell over that weekend (MSCI EM Index dropped c 50bps). This would have been to the Fund's advantage enabling assets to be purchased at lower prices.

3 CONSULTATION

- 3.3 Officers have fully consulted with the Pension Fund's advisers in preparing this report.

4 FINANCIAL CONSIDERATIONS

- 4.3 This report deals exclusively with the structure of the Council's Pension Fund.

5 COMMENTS OF THE COUNCIL SOLICITOR AND MONITORING OFFICER

- 5.1 There are no additional legal implications arising from the recommendations within this report.

Approved by: Sandra Herbert, Head of Litigation and Corporate Law, for and on behalf of Jacqueline Harris-Baker, Director of Law and Governance and Monitoring Officer.

6 OTHER CONSIDERATIONS

- 6.1 There are no Human Resource, Customer Focus, Equalities, Environment and Design, Crime and Disorder or Human Rights considerations arising from this report.

7 FREEDOM OF INFORMATION/DATA PROTECTION CONSIDERATIONS

- 7.1 This report contains confidential information which could be of a sensitive nature, disclosure of which could prejudice the commercial interest of the companies involved and those of the Council's Pension Fund.

CONTACT OFFICER:

Nigel Cook – Head of Pensions and Treasury
Corporate Resources Department, ext. 62552.

BACKGROUND DOCUMENTS:

None

Appendices

Appendix A: London Borough of Croydon Pension Fund Transition Cost Analysis

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London Borough of Croydon Pension Fund Transition Cost Analysis

Background

In October and November 2018 the London Borough of Croydon Pension Fund redeemed £65m from the LGIM (Legal and General Investment Management) Developed World ex. Tobacco Index Fund. This was used to fund £55m of investment into the LCIV (London Collective Investment Vehicle) Emerging Market Equity Fund in two equal tranches. The remaining £10m was initially taken as a buffer, to be re-invested in the LGIM fund, but the decision was taken to instead use this opportunity to raise £10m in cash. In line with LCIV funding requirements, the two investments were made just over a week apart on 26th October and 5th November

Strategy

LGIM undertook stock switches to bring assets from the existing smaller Developed World ex. Tobacco fund into their larger main index funds. While this added a level of custody costs to the exercise, the larger index funds are considerably more liquid and see more cash inflows. This helped reduce transaction costs and increased the chance of crossing our outflow with another investor's inflow to reduce spread, which would not be possible in the smaller fund.

Conversations were held with LCIV around flexibility of timing, and the possibility of taking in-specie rather than cash subscriptions, but they were only willing to take cash.

Total Cost

There are three main components to the cost of this exercise. The first are the custody costs arising from switching stock out of the Developed World ex. Tobacco Fund for units in the main index funds. The second are the spreads paid for redeeming from the LGIM funds. The third is the 35 basis point anti-dilution levy paid on the two investments into the LCIV fund.

Custody Charges	£ 3,552.00
LGIM Fund Spreads	£ 32,865.41
Anti-Dilution Levy	£ 191,828.58
Total	£228,245.99

Comparison to Cost Estimates

Prior to the restructuring LGIM provided two cost estimates for exiting the Developed World ex. Tobacco fund. The first was based on redeeming from the fund directly, while the second assumed the stock switching method described above. Both of these assumed only £55m of redemption, with the remainder being re-invested.

The estimate for exiting the Developed World ex. Tobacco fund directly was £ 49,500. For the stock switch approach custody costs were calculated as £3,740, and the cost of selling down the fund units was estimated to be between £29,400 and £49,200, dependent upon crossing. The realised LGIM cost of £32,865 therefore represents a successful outcome, with savings from crossings of £16,400.

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Croydon Council

REPORT TO:	PENSION COMMITTEE 4 December 2018
SUBJECT:	Progress Report for Quarter Ended 30 September 2018
LEAD OFFICER:	Richard Simpson Executive Director of Resources
CABINET MEMBER	Councillor Simon Hall Cabinet Member for Finance and Resources
WARDS:	All
CORPORATE PRIORITY/POLICY CONTEXT:	
<p>Sound Financial Management: Reviewing and ensuring that the performance of the Council's Pension Fund investments are in line with their benchmark and in line with the assumptions made by the Actuary.</p>	
FINANCIAL SUMMARY:	
<p>This report shows that the market value of the Pension Fund (the Fund) investments as at 30 September 2018 was £1,243.4m compared to £1,188.9m at 30 June 2018, an increase of £54.5m and a return of 4.25% over the quarter. The performance figures in this report have been compiled from data provided by each fund manager and are quoted net of fees. Independent information and analysis on the fund managers and markets have been provided by the Fund's independent investment advisor Mercer.</p>	

1	RECOMMENDATIONS
1.1	The Committee is asked to note the performance of the fund for the quarter.

2 EXECUTIVE SUMMARY

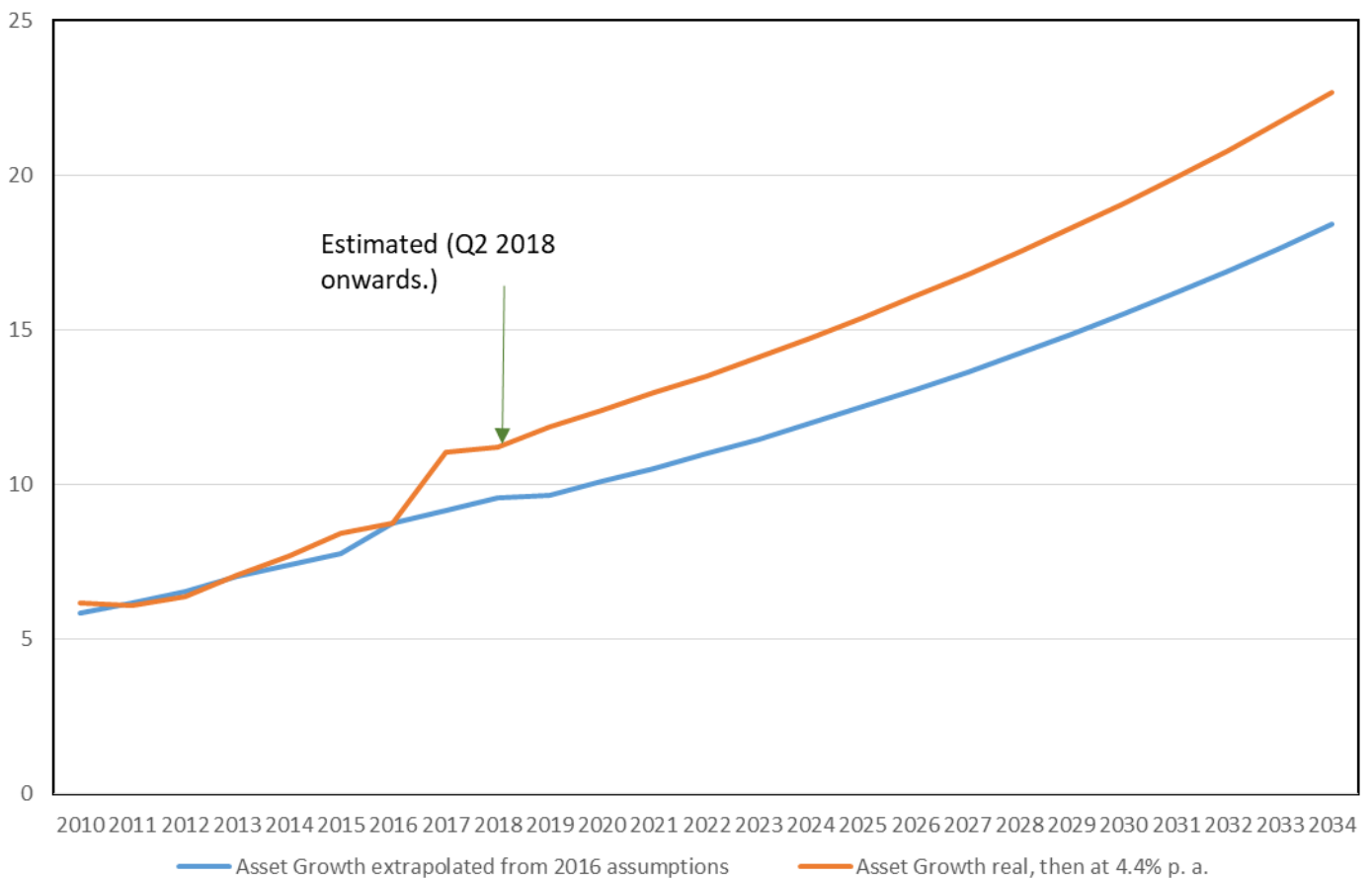
- 2.1 This report provides an update on the London Borough of Croydon Pension Fund's (the Fund's) performance for the quarter to 30 September 2018. The report falls into four parts. Section 1 addresses performance against strategic goals. The second section considers the asset allocation strategy and how that is being applied, specifically current and planned investments. The third section deals with risk management and the fourth and final section summarises the recent investment manager site visit. Detailed numeric data and commentary from the Fund's advisors is included as appendices to this report.

3 DETAIL

Section 1: Performance

- 3.1 The 2016 Triennial Actuarial Valuation used an asset outperformance assumption of 2.2% over gilt yields, meaning an asset return assumption, otherwise described as the discount rate, of 4.4%. The valuation also assumes that the funding gap will be closed over a 22 year period. However, as a risk based model has been adopted, the recovery period is less critical. In setting the Pension Fund's investment strategy, performance is measured against a benchmark return of CPI + 4% for the whole fund. Achieving this benchmark return will ensure the investments achieve a higher return than as calculated in the valuation and assuming other assumptions remain constant, the funding gap will reduce.
- 3.2 The following graph has been compiled from this information. The blue line shows the expected track of the value of assets growing in line with the 2016 valuation assumptions. This will be adjusted after subsequent valuations. The orange line shows the actual value of the Fund to date and plots the course of growth over subsequent years using the same assumptions. This measure does not take account of other variables, such as changes in demographic factors, wage inflation forecasts and other assumptions and that does not reflect changes in cash contributions nor movements in the gilt yield curve. It is valuable as a tool to help track whether the direction of travel is in the right direction.

Fund Growth Compared to Actuarial Valuation Assumptions



3.3 Details of the performance of individual components of the portfolio are summarised in Appendix A. The returns for L&G, Standard Life, Wellington and Schrodgers are calculated on a time series basis. This basis negates the effect of any cash flows made to and from a manager’s portfolio (the reason being that the timing of investments and disinvestments is not the manager’s decision) and so allows the performance of those managers to be compared fairly with their benchmarks and peers. The returns for the other managers are calculated using the Internal Rate of Return (IRR). Using the IRR considers the effect of cash flows and this is deemed appropriate for these managers as the timing of investments is determined by the manager. Due to the nature of these investments, less emphasis should be put on the performance for immature investments; Temporis, GIB, Access, North Sea Capital and M&G, and more attention should be made to the performance since inception for the more mature investments: Equitix, Knightsbridge and Pantheon. The whole of fund return uses the IRR as this is in line with the Actuary when calculating the valuation. It should be noted that the portfolio has been built on the premise that diversification mitigates the impact of return volatility, the performance of individual investments is less important than the return of the Fund in aggregate and certainly cannot be assessed over less than a full cycle, and the duration of the cycle will vary from asset to asset.

Section 2: Asset Allocation Strategy

3.4 A new asset allocation strategy was approved at the Committee meeting held on 8 September 2015 (Minute .A29/15 refers). Recognising that there are a number of factors dictating the delivery timeframe for the asset allocation, namely: the selection process and time taken to undertake due diligence; the revision of the LGPS investment regulations; and the role of the London CIV; delivering the revised asset allocation remains a work in progress.

3.5 This asset allocation will give rise to a portfolio which can be broken down as follows:

Equities including allocation to emerging markets.	42%	+/- 5%
Fixed interest	23%	+/- 5%
Alternates	34%	+/- 5%
<i>Comprised of:</i>		
Private Equity	8%	
Infrastructure	10%	
Traditional (Commercial) Property	10%	
Private Rental Sector (Residential) Property	6%	
Cash	1%	
	100%	

3.6 Progress towards revised asset allocation

To recap, since the revised asset allocation was agreed £69.2m has been disinvested from global equities and £32.2m from hedge funds. This, along with new cash to the fund has been invested; £20m in private equity, £75m in infrastructure, £25.5m in Private Rental Sector property and £16.4m in traditional property.

3.6.1 **Private Equity** – During the quarter net distributions of £0.6m were paid from our existing private equity managers and positive returns of £8.2m were generated. The current allocation to this asset class is 8.6% of the Fund. The Fund's Private Equity assets are performing well and the allocation is considered on target.

Allocation: On target.

3.6.2 **Infrastructure** – During the quarter a net contribution of £9.3m was paid to our existing managers and positive returns of £3.4m were generated in the quarter meaning the allocation percentage increased to 10.5%. The Fund's Infrastructure assets are all performing well and the allocation is on target.

Allocation: On target.

3.6.3 **Traditional Property** – During the quarter positive returns of £2.5m meant the allocation remained on target.

Allocation: On target.

3.6.4 **Private Rental Sector** - The Fund signed a commitment of £25m to the M&G UK Residential Fund in January 2016 and during the quarter ending 31 December 2016 signed a commitment for a further £35m with M&G. The first tranche of £25m was

fully drawn by 30 June 2017 and is generating positive returns. During the last quarter M&G continued to drawdown the second tranche. At 30 September 2018 £24.1m of the second tranche had been drawn. We are expecting the final £10.8m to be drawn in the next quarter as planned. The allocation increased to 3.9% over the quarter.

Allocation: The allocation will be at 5% by 31 December 2018. This is 1% below the target allocation and is due to strong performance of the fund over the previous year.

3.6.5 Global Equities – The Fund’s allocation to equities remained overweight at 51.0% which is 1.6% less than reported for the previous quarter and still outside of the agreed tolerances. Our Global Equity portfolio increased a value of £8m over the quarter despite £30m being divested. After the quarter end £55m was divested from our Global Equity portfolio and transferred to Janus Henderson managed by the London CIV in order to meet our emerging market allocation. Officers have also commenced moving a further £80m from Legal & General to PIMCO which is also managed by the London CIV. This is as agreed at the previous Pensions Committee meeting. This will reduce our Global Equity allocation to target allocation.

3.6.6 Fixed Interest – The Fund remains below the lower end of the target range in its fixed income allocation. At the previous meeting, the Pensions Committee agreed to transfer £80m from Legal and General to PIMCO, which is the fund offered by the London CIV. It was also agreed to transfer assets from the Standard Life Absolute Return Mandate (approx. £62.5m) to PIMCO.

3.6.7 The table below illustrates the movement in the Fund’s valuation during the quarter and the current asset allocation against the target.

	Valuation at 30/06/2018 £'000	Net Cashflow £'000	Gain/loss £'000	Valuation at 30/09/2018 £'000	Asset Allocation Fund Percentage	Asset Allocation Target Percentage
Equities					51.0%	42%
Legal & General FTSE4Good	162	-	41	203		
Legal & General FTSE World (Ex Tobacco)	625,106	30,090	38,583	633,599		
Fixed Interest					15.3%	23%
Standard Life	128,374	-	809	127,565		
Wellington	64,086	-	852	63,234		
Infrastructure					10.5%	10%
Access	9,559	1,000	97	10,656		
Temporis	20,863	8,530	816	30,209		
Equitix	60,262	160	1,583	62,005		
Green Investment bank	24,897	361	1,081	25,618		
I Squared	1,730	-	168	1,562		
Private Equity					8.6%	8%
Knightsbridge	23,025	1,042	1,835	25,902		
Pantheon	63,161	1,400	4,350	66,111		
Access	11,927	1,104	1,946	12,769		
North Sea	1,314	894	119	2,327		
Property					9.8%	10%
Schroders	119,969	-	2,468	122,437		
Property PRS					3.9%	6%
M&G	25,888	23,636	516	49,008		
Cash					0.8%	1%
Cash	8,576	1,564	18	10,158		
Fund Total	1,188,899	3,871	50,593	1,243,363	100%	100%

Section 3: Risk Management

- 3.9 The principle risk addressed by the Funding Strategy is that returns on investment will fall below the target asset outperformance assumption to ensure that the Pension Fund matches the value of liabilities in the future. Dependent upon that are of course a number of issues.
- 3.10 The global economy will always represent a specific risk and opportunity for the Fund and will effectively be impossible to quantify or evaluate. As each asset class, investment strategy and characteristic will be impacted differently by any number of macroeconomic scenarios it is critical to ensure that the portfolio is sufficiently diversified. This will ensure that opportunities can be exploited and downside volatility reduced as far as possible.
- 3.11 Mercer, the Fund's investment advisor, have drafted a Fund Monitoring Report, for the 3 months to 30 September 2018. These reports are included in the closed part of this Committee agenda.

Section 4: Investment Manager Visit

- 3.12 Members of the Pensions Committee visited Macquarie in September 2018. Macquarie manage the Green Investment Group Offshore Wind Fund. The Committee noted that the Fund is delivering as per our expectations.

4 CONSULTATION

- 4.1 Officers have fully consulted with the Pension Fund's advisers in preparing this report.

5 FINANCIAL CONSIDERATIONS

- 5.1 This report deals exclusively with the investment of the Council's Pension Fund and compares the return on investment of the Fund against the benchmark return.

6. COMMENTS OF THE COUNCIL SOLICITOR AND MONITORING OFFICER

- 6.1 There are no additional legal implications arising from the recommendations within this report.

Approved by: Sandra Herbert, Head of Litigation and Corporate Law, for and on behalf of Jacqueline Harris-Baker, Director of Law and Governance and Monitoring Officer.

7. FREEDOM OF INFORMATION/DATA PROTECTION CONSIDERATIONS

- 7.1 This report contains only information that can be publicly disclosed. The confidential information is reported in the closed part of the agenda.

CONTACT OFFICER:

Nigel Cook – Head of Pensions and Treasury
PEN 05062018 A

Resources Department, ext. 62552.

BACKGROUND DOCUMENTS:

Quarterly reports from each fund manager (circulated under separate cover)

Appendices:

Appendix A: London Borough of Croydon Returns to 30 September 2018

Part B appendices:

Pursuant to Schedule 12A paragraph 3: Information relating to the financial or business affairs of any particular person (including the authority holding that information), the following appendices are considered to be precluded from publication:

Appendix B: Market Background and Market View Q2 2018, Mercer

Appendix A

London Borough of Croydon fund returns for the period ending 30 September 2018

EQUITIES					
L&G Ex tobacco	Quarter	1 year	3 year	5 year	inception
Fund	6.3%				11.4%
Benchmark	6.3%				11.6%
FIXED INTEREST					
Standard Life	Quarter	1 year	3 year	5 year	inception
Fund	-0.6%	-0.7%	2.5%	2.9%	4.1%
Benchmark	-0.3%	0.1%	2.6%	3.4%	4.3%
Wellington	Quarter	1 year	3 year	5 year	inception
Fund	-1.3%	1.5%	3.5%	4.9%	5.9%
Benchmark	-1.4%	0.4%	3.5%	4.9%	5.6%
INFRASTRUCTURE					
Equitix	Quarter	1 year	3 year	5 year	inception
Fund	2.7%	17.4%	11.1%	12.4%	14.3%
Benchmark	2.0%	7.4%	7.1%	6.5%	7.3%
Temporis	Quarter	1 year	3 year	5 year	inception
Fund	1.0%	12.6%			6.9%
Benchmark	2.0%	7.4%			7.4%
GIB	Quarter	1 year	3 year	5 year	inception
Fund	4.6%	9.3%			9.5%
Benchmark	2.0%	7.4%			7.6%
Access	Quarter	1 year	3 year	5 year	inception
Fund	1.0%	6.3%			3.8%
Benchmark	2.0%	7.4%			7.4%
PRIVATE EQUITY					
Knightsbridge	Quarter	1 year	3 year	5 year	inception
Fund	8.7%	18.6%	16.3%	18.3%	14.4%
Benchmark	2.0%	7.4%	7.1%	6.5%	7.1%
Pantheon	Quarter	1 year	3 year	5 year	inception
Fund	18.7%	22.3%	21.5%	17.1%	13.9%
Benchmark	2.0%	7.4%	7.1%	6.5%	7.2%
Access	Quarter	1 year	3 year	5 year	inception
Fund	22.2%	28.1%			17.7%
Benchmark	2.0%	7.4%			7.4%
North Sea Capital	Quarter	1 year	3 year	5 year	inception
Fund	6.4%	-6.0%			-8.4%
Benchmark	2.0%	7.4%			7.6%
PROPERTY					
Schroders	Quarter	1 year	3 year	5 year	inception
Fund	2.1%	9.9%	6.5%	10.9%	10.1%
Benchmark	1.6%	8.9%	7.1%	10.4%	9.3%
PROPERTY PRS					
M&G	Quarter	1 year	3 year	5 year	inception
Fund	0.66%	3.44%			-0.29%
Benchmark	1.71%	7.00%			7.00%
Total Fund					
	Quarter	1 year	3 year	5yr	inception
Fund	4.25%	11.42%	12.25%	11.04%	8.14%
CPI + 4%	1.74%	6.40%	6.10%	5.48%	6.27%

Returns are net of fees and annualised apart from for the last quarter

Returns for Equity, Fixed Interest and Property Funds are calculated on a time weighted basis.

Returns for Infrastructure, Private Equity, Property PRS funds and the Total return are calculated on an Internal rate of return basis.

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