

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.