MUNICIPAL YEAR 2019/2020 REPORT NO. 147

MEETING TITLE AND DATE:
Pension Policy & Investment Committee
21st November 2019

REPORT OF:
Director of Finance

Contact officer and telephone number:

Bola Tobun – 020 8379 6879

E mail: Bola.Tobun@enfield.gov.uk

Agenda – Part:	**Item: 5**
Subject: Quarterly Investment Report for September 2019 **Wards: All** **Key Decision No:**	
Cabinet Member consulted:	

1. EXECUTIVE SUMMARY

This report informs Members of the performance of the Pension Fund and its investment managers for the last quarter.

Over the quarter to 30 September 2019 the Fund posted a positive return of c.3%	Over the three-month period to 30 September 2019 all Equity markets delivered positive returns in both local currency and sterling terms, except Emerging Market equities, that posted a negative return in local currency. The Fund outperformed its benchmark by 0.2%. Fund value was £1.264bn, a £41m increase from the June quarter end.
For the quarter thirteen mandates matched/achieved benchmark return	For this quarter, thirteen mandates matched or achieved returns above the set benchmark. Eight out of twenty-one mandates underperformed their respective benchmark by producing a return below cash return. The underperforming portfolios are Lansdowne, Longview, CFM Stratus, York capital, Western, Insight Bonds, LCIV Baillie Gifford and LCIV Henderson.
The Fund's investments out performed its benchmark over the 12-month period	Over the twelve-month period to 30 September 2019, the Fund outperformed its benchmark by 0.75%. For the year to 30 September 2019, the following portfolios generated significant amount of unrealised losses: Lansdowne -15%, York Capital -11% and Insight Bonds -7%.
Longer-term performance, the Fund outperformed its benchmark return	Looking at the longer-term performance, the three-year return for the Fund was 1.6% per annum above its benchmark return and for over five years, the Fund posted a strong return of 7.9% outperforming the benchmark return of 6.2% by 1.7%.
Currency appreciation is a major factor in performance	The appreciation of sterling versus the US dollar over the quarter decreased the value of dollar denominated holdings. The active equity managers have exposures to various currencies as they are all global mandates.
Fund is broadly in line with benchmark weightings	The distribution of the Fund's assets amongst the different asset classes is broadly in line with the strategic benchmark weight, albeit there is a need to rebalance the assets and equities is mildly overweight. The overweight position in equities has helped the fund's performance in recent months.

2. RECOMMENDATIONS

2.1. Members are recommended to note the contents of this report.

3. BACKGROUND

3.1. The Pension Fund Regulations require that the Council establishes arrangements for monitoring the investments of the Fund. It considers the activities of the investment managers and ensures that proper advice is obtained on investment issues.

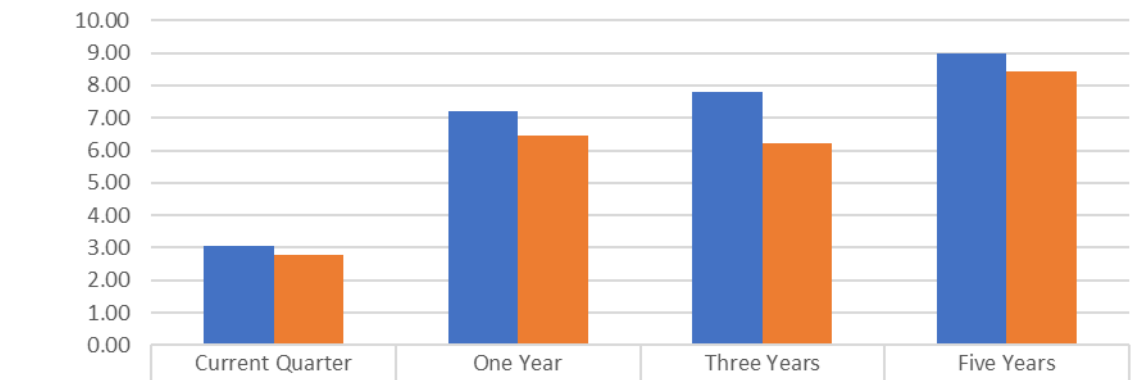
3.2. Officers and fund advisers meet regularly with investment managers to discuss their strategy and performance and if considered necessary may recommend that investment managers are invited to explain further to the Pension Policy & Investment Committee.

INVESTMENT PERFORMANCE

3.3. The overall value of the Fund at 30 September 2019 stood at £1,264m which is a substantial increase of £41m from its value of £1,223m as at 30 June 2019.

3.4. The fund outperformed the benchmark this quarter by posting a return of 3.04% against benchmark return of 2.79%. The twelve-month period sees the fund also ahead its benchmark by 0.75%.

3.5. Looking at the longer-term performance, the three years return for the Fund was 7.79%, which was 1.57% per annum ahead its benchmark return. Over the five years, the Fund posted a return of 8.98% outperforming the benchmark return of 8.44% by 0.54% per annum, as shown on the graph below.



	Current Quarter	One Year	Three Years	Five Years
Fund	3.04	7.20	7.79	8.98
Benchmark	2.79	6.45	6.21	8.44

3.6. For this reporting quarter, thirteen out of twenty-one mandates delivered positive return, matched or achieved returns above the set benchmark. The eight mandates that posted returns that did not meet their benchmarks were Lansdowne lagging its benchmark by 2.3%; Henderson lagging its benchmark by 3.6%; LCIV Baillie Gifford lagging its benchmark by 2.6%; York Capital lagging its benchmark by 2.9%; CFM Stratus lagging its benchmark by 2.8%; BlackRock

Property lagging its benchmark by 0.2%; Western lagging its benchmark by 0.33%; and Insight lagging its benchmark by 1.7%.

3.7. For the 12 months to September 2019, six out of seventeen mandates underperformed their respective benchmarks or targets. The mandates that delivered negative returns or underperformed its benchmark/target were LCIV Baillie Gifford, Legal & General Property, Blackrock Property, Insight Bonds, York Capital and Lansdowne. Lansdowne and York Capital generated significant amount of unrealised losses of -15% and -11% respectively for one year to 30 September 2019.

INTERNAL CASH MANAGEMENT

3.8. Cash is held by the managers at their discretion in accordance with limits set in their investment guidelines, and internally by Enfield Council to meet working cashflow requirements, although transfers can be made to Fund managers to top up or rebalance the Fund.

3.9. The Pension Fund cash balance is invested in accordance with the Council's Treasury Management strategy agreed by Full Council in February 2019, which is delegated to the Executive Director of Resources to manage on a day to day basis within the agreed parameters.

3.10. The cash balance as at 30 September 2019, was £46.905m in short term deposits and money market funds. £24.567m with Goldman Sachs, £17.347m with Northern Trust and £5m with Close Brothers.

CURRENCY ANALYSIS

3.11. The appreciation of sterling versus the US dollar over the quarter decreased the value of dollar denominated holdings.

3.12. At this reporting quarter, the Fund has 6.4% of total assets exposure to the euro, 33.3% to US dollar, 2.2% to yen and 5.3% to other currencies within its portfolio. The active equity managers have exposures to various currencies as they are all global mandates, and AON, the Fund Investment Consultant have approximated the currency exposures based on the geographical split of the underlying investments.

3.13. Adams Street, York and Davidson Kempner are US dollar denominated whilst Antin is euro-denominated. The Lansdowne, CFM, BlackRock, CBRE, Western, M&G Inflation Opportunities, Legal & General, Brockton, Insight and IPPL mandates are assumed to have no direct exposure to foreign currencies as they are either hedged to sterling or are sterling share classes.

3.14. US dollar exposure of 33.3% of the total assets is the largest foreign currency risk for the Fund. For example, a 1% foreign currency appreciation (or depreciation) for the Funds' US dollar denominated assets will increase (or decrease) by £4.2m, for Euro denominated assets in our Fund will increase (or decrease) by £0.9m and Yen denominated assets will increase (or decrease) by £0.2m.

3.15. It is therefore worth noting that movements in currencies may either contribute to or be caused by factors that move other asset classes. For example, the US dollar may appreciate at times of stress which could coincide with a fall in the value of the Fund's equity holdings.

ASSET ALLOCATION

3.16. The current strategic weight of asset distribution and the Fund's assets position as at 30 September 2019 are set out below:

Asset Class	Strategic asset allocation as at April 2019 (%)	Fund Position as at 30 Sept 2019 (%)	Variance as at 30 Sept 2019 (%)	Variance as at 30 Sept 2019 (£m)
Equities	35.0	39.9	4.9	61.936
Private Equities	5.0	6.1	1.1	13.904
Total Equities	**40.0**	**46.0**	**6.0**	**75.840**
Hedge Funds	10.0	9.7	(0.3)	(3.792)
Property	10.0	6.0	(4.0)	(50.560)
Infrastructure	6.0	5.1	(0.9)	(11.376)
Bonds	24.0	21.8	(2.2)	(27.808)
Inflation protection illiquid	10.0	7.7	(2.3)	(29.072)
Cash	0.0	3.7	3.7	46.768
Total Equities	**100.0**	**100.0**		

3.17. The table above indicates the Fund is overweight by 3.7% in Cash and 6% in Equities; but the Fund has underweight position of 4% in Property, Bonds and Indexed linked gilts underweight position of 0.3%, Inflation protection illiquid underweight position of 2.3%, Hedge Funds with 1.9% underweight position and Infrastructure with 1%. There is a need for assets rebalancing to their strategic weights, the consideration for this could be included in the upcoming investment strategy review for the Fund.

3.18. The Fund initial triennial valuation result was very favourable with an outcome of 103% funding level. This means as at 31st March 2019 valuation, the Fund is in surplus. The next step is for the Committee to have a discussion with the actuary to agree the parameters to set employers contribution going forward. Thereafter the Fund Investment Consultant would be commissioned to carry out investment strategy review to incorporate the Fund's new investment beliefs integrated with ESG considerations.

3.19. Approximately 15% of the equity portfolio is being managed passively by BlackRock. The remainder is being managed on an active basis, with the largest share of 9.8% with MFS, 6.6% with Longview and 6.4% with LCIV Baillie Gifford.

3.20. In aggregate, 7.2% of the Fund's equity portfolio is allocated to Emerging Markets. As at 30 September 2019, the MSCI All Country World Index had a 11.5% exposure to Emerging Markets.

3.21. Asset allocation is determined by several factors including: -

i) The risk profile - there is a trade off between the returns that can be obtained on investments and the level of risk. Equities have higher potential returns, but this is achieved with higher volatility. However, the Fund remains open to new members and able to tolerate the volatility, allowing it

to target higher returns, which in turn reduces the deficit quicker and should eventually lead to lower contribution rates by employers.

ii) The age profile of the Fund - the younger the members of the Fund, the longer the period before pensions become payable and investments must be realised for this purpose. This enables the Fund to invest in more volatile asset classes because it has the capacity to ride out adverse movements in the investment cycle.

iii) The deficit recovery term / the surplus amortisation period - Most LGPS funds are fully Funded or almost 100% funded because of great investment returns but being tampered mildly by increasing life expectancy. The actuary determines the period over which the deficit is to be recovered and considers the need to stabilise the employer's contribution rate. For 2016 triennial valuation the actuary had set a 19 year deficit recovery term for the Council, which enables a longer term investment perspective to be taken. For this 2019 initial valuation result, the actuary also used 19 years as the target of reducing the funding ratio, to illustrate the surplus amortisation.

3.22. Individual managers have discretion within defined limits to vary the asset distribution. The overweight position in equities has helped the fund's performance in recent months.

Key Developments

3.23. The lead portfolio manager of the Janus Henderson Emerging Market Equity strategy, Glen Finegan has resigned from Janus Henderson, along with a number of his team members. Aon, the Fund Investment consultant downgraded their rating on the strategy to Sell following this news. This strategy is the London CIV sub fund for Emerging Market Equity Fund and London CIV have now appointed JP Morgan as a replacement for Janus Henderson for managing this sub fund.

3.24. The London CIV have placed CQS on 'Watch', based on a number of concerns they have regarding underperformance relative to target, staff changes, and concerns over the strategy. CQS are currently the only Multi-Asset Credit (MAC) manager within the London CIV MAC Fund. The London CIV is currently consulting with the current investors to ascertain their need for this product. LCIV do have the ability to add / remove / blend the underlying managers. Aon remain supportive of the Pension Fund investing in a MAC style mandate in order to diversify the Fund's bond portfolio by extending the opportunity set.

3.25. On 23 October 2019 Brockton informed investors that the manager is cancelling part of investors' undrawn commitments with effect from 31 October 2019. This reduces the Fund's undrawn commitment from c.£14.7m to c.£10.2m. Whilst performance and asset management within the fund remain strong. AON to provide further comments and views as soon as they received further information from Brockton. before.

4. ALTERNATIVE OPTIONS CONSIDERED

4.1. The Pension Fund Regulations require that the Council establishes arrangements for monitoring the investments of the Fund. It considers the activities of the investment managers and ensures that proper advice is obtained on investment issues.

5. REASONS FOR RECOMMENDATIONS

5.1. The report informs the Pension Policy and investment Committee of the performance of pension fund managers and the overall performance of the Enfield Pension Fund.

6. COMMENTS FROM OTHER DEPARTMENTS

6.1 Financial Implications

This is a noting report which fulfils the requirement to report quarterly performance of the Pension Fund investments portfolio to the Pension Policy and Investment Committee. There are no direct financial implications arising from this report, however the long-term performance of the pension fund will impact upon pension contribution rates set by this Committee.

6.2 Legal Implications

a) The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 govern the way in which administering authorities should manage and make investments for the fund. There are no longer explicit limits on specified types of investment and instead administering authorities should determine the appropriate mix of investments for their funds. However, administering authorities must now adhere to official guidance; broad powers allow the Government to intervene if they do not. Under regulation 8, the Secretary of State can direct the administering authority to make changes to its investment strategy; invest its assets in a particular way; that the investment functions of the authority are exercised by the Secretary of State and that the authority complies with any instructions issued by the Secretary of State or their nominee.

b) The Council must take proper advice at reasonable intervals about its investments and must consider such advice when taking any steps in relation to its investments.

c) The Council does not have to invest the fund money itself and may appoint one or more investment managers. Where the Council appoints an investment manager, it must keep the manager's performance under review. At least once every three months the Council must review the investments that the manager has made and, periodically, the Council must consider whether or not to retain that manager.

d) One of the functions of the Pension Policy & Investment Committee is to meet the Council's duties in respect of investment matters. It is appropriate, having regard to these matters, for the Committee to receive information about asset allocation and the performance of appointed investment managers. The Committee's consideration of the information in the report contributes towards the achievement of the Council's statutory duties.

e) When reviewing the Pension Fund Investment Performance, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty). The Committee may take the view that good, sound investment of the Pension Fund monies will support compliance with the Council's statutory duties in respect of proper management of the Pension Fund.

7. KEY RISKS

7.1 Any form of investment inevitably involves a degree of risk.

a) To minimise risk the Pension Policy and Investment Committee attempts to achieve a diversification portfolio. Diversification relates to asset classes and management styles.

b) The monitoring arrangement for the Pension Fund and the work of the Pension Policy & Investment Committee should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

Background Papers – None

Appendices – The below appendices are attached electronically but not in the main pack.

- Appendix 1 – Northern Trust Performance Review Report
- Appendix 2 – AON Quarterly Report
- Appendix 3 – London CIV Sub-Funds Quarterly Report

Officer contact details for documents:

Bola Tobun - Pension &Treasury Manager
Tel no. 020 8364 6879
Civic Centre, B Block South
Silver Street, Enfield
London EN1 3XF