MUNICIPAL YEAR 2019/2020 REPORT NO. 230

MEETING TITLE AND DATE: Pension Policy & Investment Committee 27th February 2020 **REPORT OF:** Director of Finance Contact officer and telephone number: Bola Tobun – 020 8379 6879 E mail: Bola.Tobun@enfield.gov.uk	**Agenda – Part:1** | **Item: 7** **Subject: Quarterly Investment Report for December 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 31 December 2019 the Fund posted a negative return of c.-0.1%	Over the three-month period to 31 December 2019 all Equity markets delivered positive returns in both local currency and sterling terms. The Fund underperformed its benchmark by -0.6%. Fund value was £1.263bn, reduced by £1m over this reporting quarter end.
For the quarter thirteen mandates matched/achieved benchmark return	For this quarter, twelve mandates matched or achieved returns above the set benchmark. Eight out of twenty mandates underperformed their respective benchmark by producing a return below cash return. The underperforming portfolios are Brockton, CFM Stratus, York capital, Adams Street, LCIV Henderson, MFS, M & G Inflation and Davidson Kempner.
The Fund's investments out performed its benchmark over the 12-month period	Over the twelve-month period to 31 December 2019, the Fund outperformed its benchmark by 0.4%. For the year to 31 December 2019, the following portfolios generated significant amount of unrealised losses: Adam Street -17%, York Capital -11% and Lansdowne -2%.
Longer-term performance, the Fund outperformed its benchmark return	Looking at the longer-term performance, the three-year return for the Fund was 0.7% per annum above its benchmark return and for over five years, the Fund posted a strong return of 8.2% outperforming the benchmark return of 7.6% by 0.6%.
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.

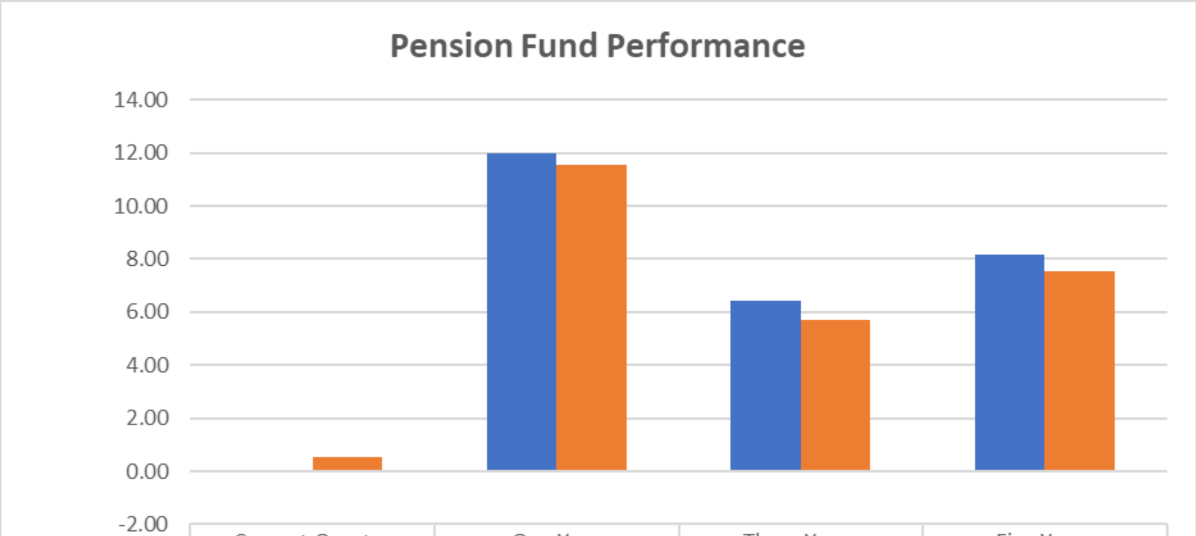
3.2. Officers and fund advisers meet regularly with investment managers to discuss their strategy and performance and if considered necessary may recommend that investment managers are invited to explain further to the Pension Policy & Investment Committee.

INVESTMENT PERFORMANCE

3.3. The overall value of the Fund at 31 December 2019 stood at £1,263m which is a slight reduction of £1m from its value of £1,264m as at 30 September 2019.

3.4. The fund underperformed the benchmark this quarter by posting a return of -0.06% against benchmark return of 0.53%. The twelve-month period sees the fund slightly ahead its benchmark by 0.4%.

3.5. Looking at the longer-term performance, the three years return for the Fund was 6.44%, which was 0.72% per annum ahead its benchmark return. Over the five years, the Fund posted a return of 8.15% outperforming the benchmark return of 7.56% by 0.59% per annum, as shown on the graph below.



	Current Quarter	One Year	Three Years	Five Years
Fund	-0.06	11.96	6.44	8.15
Benchmark	0.53	11.55	5.72	7.56

3.6. For this reporting quarter, twelve out of twenty mandates delivered returns, matching or achieving returns above the set benchmark. The eight mandates that posted negative returns or did not meet their set benchmarks were York capital lagging its benchmark by -7.36%, Adams Street lagging its benchmark by

-9%, LCIV Henderson lagging its benchmark by -3.8%, M & G Inflation lagging its benchmark by-3%, CFM Stratus lagging its benchmark by -2.5%, MFS lagging its benchmark by-1.5%, Brockton lagging its benchmark by -0.09%, and Davidson Kempner lagging its benchmark by-0.07%.

3.7. For the 12 months to December 2019, six out of eighteen mandates underperformed their respective benchmarks or targets. The mandates that delivered negative returns or underperformed its benchmark/target were LCIV Henderson, LCIV Longview, Blackrock UK Property, Insight Bonds, York Capital and Lansdowne. LCIV Henderson and York Capital generated significant amount of unrealised losses of -8.4% and -10.7% respectively for one year to 31 December 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 31 December 2019, was £46.858m in short term deposits and money market funds. £27.740m with Goldman Sachs, £14.118m 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 6.3% of total assets exposure to the euro, 33.5% to US dollar, 2.2% to yen and 4.9% 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 Capital 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 33.5% 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 £0.8m and Yen denominated assets will increase (or decrease) by £0.3m.

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 31 December 2019 are set out below:

Asset Class	Strategic asset allocation as at April 2019 (%)	Fund Position as at 31 Dec 2019 (%)	Variance as at 31 Dec 2019 (%)	Variance as at 31 Dec 2019 (£m)
Equities	35.0	40.7	5.7	71.999
Private Equities	5.0	5.5	0.5	6.316
Total Equities	**40.0**	**46.2**	**6.2**	78.315
Hedge Funds	10.0	9.7	(0.3)	(3.789)
Property	10.0	6.1	(3.9)	(49.262)
Infrastructure	6.0	5.4	(0.6)	(7.578)
Bonds	24.0	21.6	(2.4)	(30.315)
Inflation protection illiquid	10.0	7.7	(2.3)	(29,052)
Cash	0.0	3.3	3.3	41.684
Total Equities	**100.0**	**100.0**		

3.17. The table above indicates the Fund is overweight by 3.3% in Cash and 6.2% in Equities; but the Fund has underweight position of 4% in Property, Bonds and Indexed linked gilts underweight position of 2.4%, Inflation protection illiquid underweight position of 2.3%, Hedge Funds with 0.3% underweight position and Infrastructure with 0.6%. There is a need for assets rebalancing to their strategic weights, the consideration for this will be included in the upcoming investment strategy review for the Fund.

3.18. The Fund 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 outcome of Enfield Pension Fund of 103% funding level has put the Fund in a favourable position and it is worth noting that the strong 2016-2019 asset performance was due to high exposures to (strongly performing) overseas equities.

3.19. The next step, is for the Fund Investment Consultant to carry out an investment strategy review, incorporating the Fund's new investment beliefs. Bearing in mind that the high recent asset growth also leads to lower return expectations hence higher primary contribution.

3.20. 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, followed by 6.9% with LCIV Longview, 6.8% with LCIV Baillie Gifford and 2.2% in LCIV EM.

3.21. As at 31 December 2019, the MSCI All Country World Index had a 12.2% exposure to Emerging Markets. In aggregate, the Fund's equity portfolio has £30.9m which is c.2.5% of the total assets invested in Emerging Markets.

3.22. 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 this 2019 valuation, the actuary has used 16 years as the target of reducing the funding ratio, to illustrate the surplus amortisation.

3.23. 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

3.24. York Capital Management announced in December 2019 the decision to liquidate the York Credit Opportunities Fund held within the portfolio. Following the liquidation announcement, The Fund Investment Consultant research team have downgraded the York fund to a "Sell" rating and have recommended a full redemption from this fund. As background, York made the decision to liquidate the York Credit Opportunities fund after receiving significant redemptions through 2020, which, given the portfolio's high concentration in illiquid post reorganization equity positions, would have put remaining investors at an unfair disadvantage. While investors have been given the option to roll over their redemption proceeds into the York Global Credit Income Fund, this fund has a different investment objective and would not be suitable as a direct replacement.

3.25. Franklin Templeton, a global leader in asset management, announced that it is purchasing Legg Mason and its affiliates, including Western Asset (WA). WA was an integral part of the discussions leading up to this deal, and Franklin Templeton shares WA commitment to upholding Western Asset's full investment independence and organisational autonomy. WA support the transaction wholeheartedly. There will be no change to our relationship team, our investment team, the Western Asset leadership team nor their investment philosophy or process as a result of this acquisition. The combined company will have an unparalleled global footprint and breadth of investment offerings as one of the world's largest active managers with over $1.5 trillion in assets under management.

3.26. M&G announced in January that Ben Jones, Head of Long Income at M&G, had left the business at the end of 2019 with immediate effect. The Fund invests in the

M&G Inflation Opportunities Fund, which has holdings in another M&G fund where Mr Jones was the co-Fund Manager (the M&G Secured Property Income Fund). M&G has made a number of role changes following Mr. Jones's exit, promoting a number of long serving team members. The Fund Investment Consultant has no concern over the changes and do not recommend any action is taken and there have been no changes to their in-house ratings for the M&G Inflation Opportunities Fund.

3.27. The London CIV Emerging Market equity fund was previously managed by Janus Henderson. The lead portfolio manager of the Janus Henderson fund, Glen Finnegan, resigned from Janus Henderson, along with a number of his team members. The Fund Investment Consultant downgraded their rating on the strategy to 'Sell' in October 2019 following this news. London CIV have appointed JP Morgan for the Emerging Market Equity fund and the portfolio was transitioned to the new manager on 11 October 2019.

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 – AON Quarterly Report
- Appendix 2 – London CIV Sub-Funds Quarterly Report

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