Havering
LONDON BOROUGH

PENSIONS COMMITTEE **12 January 2021**

Subject Heading:	**PENSION FUND PERFORMANCE MONITORING FOR THE QUARTER ENDED SEPT 2020**
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Policy context:	Pension Fund Manager performance is regularly monitored to ensure investment objectives are met.
Financial summary:	This report comments upon the performance of the Fund for the period ended 30 SEPT 2020

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

This report provides an overview of: Fund investment performance, Manager Monitoring and any relevant Local Government Pension Scheme (LGPS) updates for the quarter ending **30 September 2020**. Significant events that occur after production of this report will be addressed verbally at the meeting.

The Fund grew in value by 2.74% over this quarter after the college merger transfer is taken in account. The Fund is now overachieving both its 12 month tactical and strategic benchmark.

The general position of the Fund is considered plus other matters including any current issues as advised by Hymans.

The manager attending the meeting will be from:

London CIV
Hymans will discuss the managers' performance after which the manager will be invited to join the meeting and make their presentation.

Hymans and Officers will discuss with Members any issues arising from the monitoring of the other managers

RECOMMENDATIONS

That the Committee:

1) Consider Hymans Market Background and Strategic Overview and Manager Performance Report (Appendix A)
2) Consider Hymans Performance Report and views (Appendix B **Exempt)**
3) Receive presentation from the London CIV for the Multi Asset, UK Equities funds and Absolute Return fund on the LCIV platform (Appendix C – **Exempt)**
4) Consider the quarterly reports sent electronically, provided by each investment manager.
5) Note the analysis of the cash balances

REPORT DETAIL

1. Elements from Hymans report which are deemed non-confidential can now be found in **Appendix A.** Opinions on Fund manager performance will remain as exempt and shown in **(Appendix B).**

2. When appropriate more topical LPGS news that may affect the Pension Fund will now be included.

3. We welcome any feedback and suggestions if this helps members gain a better understanding of the reports.

4. BACKGROUND

a. The Committee adopted an updated Investment Strategy Statement (ISS) in July 2020.

b. The objective of the Fund's ISS is to deliver a stable long-term investment return in excess of the expected growth in the Fund's liabilities

c. The Fund's assets are monitored quarterly to ensure that the long term objective of the ISS is being delivered.

d. We measure returns against tactical and strategic benchmarks:

e. **Tactical Benchmark -** Each manager has been set a specific (tactical) benchmark as well as an outperformance target against which their performance will be measured. This benchmark is determined according to the type of investments being managed. This is not directly comparable to the strategic benchmark as the majority of the mandate benchmarks are different but contributes to the overall performance.

f. **Strategic Benchmark** - A strategic benchmark has been adopted for the overall Fund of Index Linked Gilts + 1.8% per annum. This is the expected return in excess of the fund's liabilities over the longer term and should lead to an overall improvement in the funding level. The strategic benchmark measures the extent to which the Fund is meeting its longer term objective of reducing the Fund's deficit.

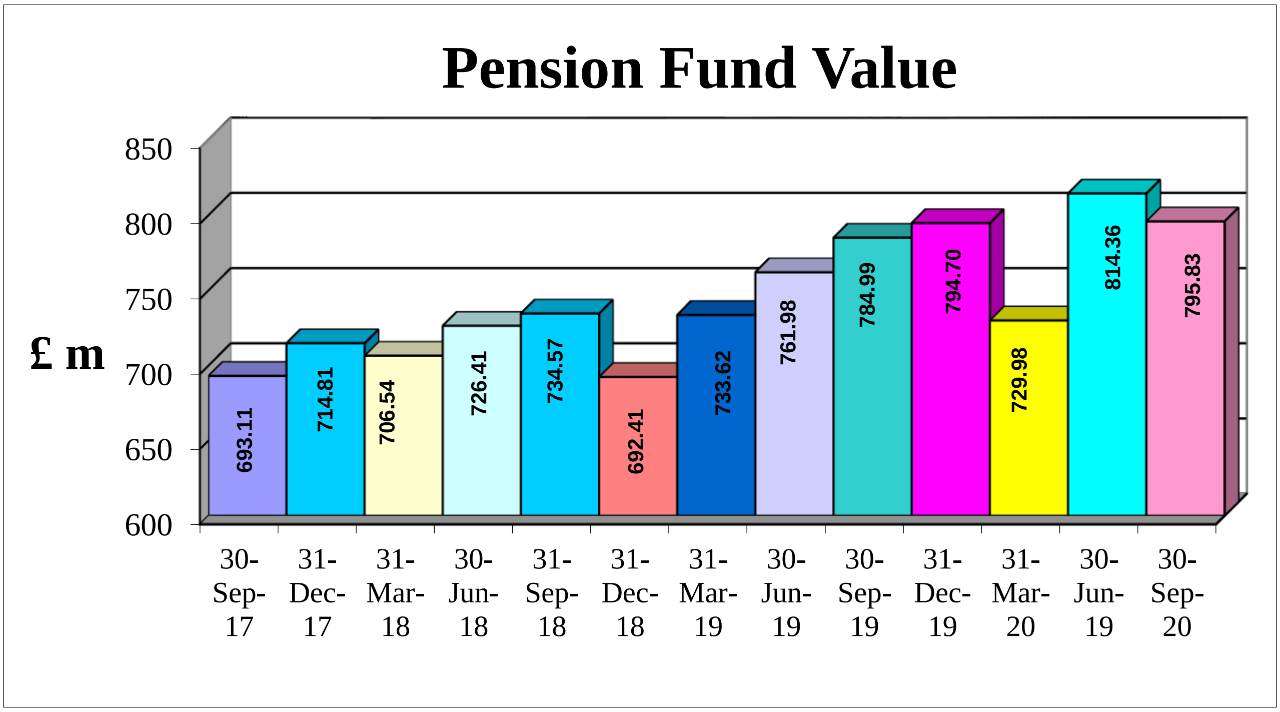
5. PERFORMANCE

a. Based on information supplied by our performance measurers, Northern Trust, the total combined fund value at the close of business on 30 September 2020 was **£795.83m.** This compares with a Fund value of £814.36m at the 30 June 2020; a **decrease of £-18.53m, (-2.98%)**. Movement in the Fund value is attributable to a decrease in assets of £-3.35m and a decrease in cash of -£15.18m. Internally managed cash level stands at **£9.12m** of which an analysis follows in this report. It should be noted that in this quarter the Fund disinvested £25.5m assets and £15.0m cash for the settlement of the college merger. When taking this into account the Fund did much better than the previous figures suggest, making an increase of £22m (2.74%) in this quarter – see table below.

	£'000s	**%**
FUND VALUE JUNE 20	**814.36**	
MINUS DISINVESTMENT COLLEGE MERGER-JULY 20	-40.5	
	773.86	
FUND VALUE SEPT 20	795.83	
FUND INCREASE IN VALUE	**21.97***	**2.74***

*figures above are rounded, % increase adjusted to agree to Northern Trust performance figure

Chart 1 – Pension Fund Values



b. The overall net performance of the Fund against the new **Combined Tactical Benchmark** (the combination of each of the individual manager benchmarks) follows:

Table 1: Quarterly Performance

	Quarter to 30.09.20	12 Months to 30.09.20	3 Years to 30.09.20	5 years to 30.09.20
	%	%	%	%
Fund	2.74	5.43	5.95	8.38
Benchmark	1.32	3.04	5.39	6.79
*Difference in return	1.42	2.39	0.55	1.59

Source: Northern Trust Performance Report
Totals may not sum due to geometric basis of calculation and rounding

c. The overall net performance of the Fund against the **Strategic Benchmark** (i.e. the strategy adopted of Gilts + 1.8% Net of fees). The strategic benchmark return reflects the historic funding approach. Since the strategic benchmark return relates to the expected change in the value of the Fund's liabilities, it is mainly driven by the assumed level of investment return used by the Actuary.

Table 2: Annual Performance

	Quarter to 30.09.20	**12 Months to 30.09.20**	**3 Years to 30.09.20**	**5 years to 30.09.20**
	%	**%**	**%**	**%**
Fund	2.74	5.43	5.95	8.38
**Benchmark	-1.72	2.20	8.24	9.36
*Difference in return	4.46	3.23	-2.29	-0.98

Source: Northern Trust Performance Report

**Totals may not sum due to geometric basis of calculation and rounding.*

*** Negative to be addressed as per note 5c above.*

d. Further detail on the Fund's investment performance is detailed in **Appendix A** in the performance report which will be covered by the Investment Adviser (Hymans).

6. CASH POSITION

a. An analysis of the internally managed cash balance of **£9.115m** follows:

Table 3: Cash Analysis

CASH ANALYSIS	**2018/19 31 Mar 19**	**2019/20 31 Mar 20**	**2020/21 30 Sept 20**
	£000's	£000's	£000's
Balance B/F	**-17,658**	**-13,698**	**-23,056**
Benefits Paid	37,954	38,880	19,450
Management costs	1,490	1,107	429
Net Transfer Values	1,543	-2,789	13,766
Employee/Employer Contributions	-44,804	-47,508	-20,325
Cash from/to Managers/Other Adj.	7,925	1,154	723
Internal Interest	-148	-202	-102
Movement in Year	**3,960**	**-9,358**	**13,941**
Balance C/F	**-13,698**	**-23,056**	**-9,115**

b. Members agreed the updated cash management policy at its meeting on the 17 September 2019. The policy sets out that the target cash level should be £6m but not fall below the de-minimus amount of £3m or exceed £8m threshold. This policy includes drawing down income from the bond and property manager when required. Any excess cash above the £8m thresholds can be considered for reinvestment or settlement of capital calls.

c. The cash management policy includes a discretion that allows the Statutory S151 officer to exceed the target level to meet foreseeable payments i.e. such as the college transfer

7. REPORTING ARRANGEMENTS

a. In line with the reporting cycle, the Committee will see one Fund Manager at each Committee meeting unless there are performance concerns for individual managers. Individual Fund Manager Reviews are attached in Hymans performance report at **Appendix A.**

b. The full version of all the fund manager's quarterly report are distributed electronically prior to this meeting. Where applicable, quarterly voting information, from each Investment Manager, detailing the voting history of the Investment Managers is also included in the Manager's Quarterly Report.

c. The Fund Manager attending this meeting is the London CIV for the funds Multi Asset, UK Equities and Absolute Return within the LCIV platform; their presentation can be found at Appendix C (Exempt).

8. FUND UPDATES:

8.1 Changes made since the last report and forthcoming changes/events:

a. The Fund has continued to fund capital draw down requests: £0.91m Churchill, £0.74m Permira and £2.03m Stafford.

b. Following the Committees decision on the 1 October 2020 to make a €20m (c. £18m) commitment to the latest vintage of the Stafford Fund (SISF IV), officers have completed the on-boarding paperwork.

c. Members received training on the merits of Multi Factor Investing from Hymans and Legal & General and Hymans will prepare recommendations for members to consider at the next meeting.

d. Officers had client performance meetings with both Private Debt managers - Churchill on the 5 November and Permira on the 10 November 2020. Both provided investment activity over the year to Q3 2020 and their fund positioning and actions taken in respect of the impact of COVID-19.

8.2 London Collective Investment Vehicle (LCIV) - LCIV is the mandatory asset pool for the Fund and updates will be covered here as follows:

8.2.1 LCIV meetings

a. Business update meetings (via WebEx) - took place on 17 September 2020,16 October 2020, 19 November and 17 December - A range of topics covered included:

- Chief Investment Officer – covered current Fund offering, Fund performance, update on funds for which enhanced monitoring is in place and the pipeline for new fund launches.
- Presentation from Pensions & Investment Research Consultants (PIRC) on the 2019/20 universe performance and asset allocations.
- Discussion panel on the topic of Investing in Low Carbon Passive Equity Funds
- Overview of the Manager Selection process
- Update from the Chief Operating Officer covering:
  i. Key themes for the MTFS and Annual Budget for 2021/22.
  ii. Funding Review and Cost Benchmarking
  iii. Summary of estimated gross and net cost savings to March 2020 that was submitted to MHCLG in September 2020. Net cumulative fee savings estimated at £70m.
- The Board and the Shareholder Committee have now approved the Budget for 2021/22 and this will be presented to the General Meeting in January for formal shareholder approval
- Discussion on the topic of identifying long term risks for the fund, in particular to Asset challenges, External Challenges and Investment Challenges. A short survey was issued after the meeting which officers responded to.
- Governance review update and progress made to date.
- ESG integration into fixed income and ESG policy implementation.
- Comparison of LCIV Infrastructure, LCIV Renewables and the London Fund presented.

b. Meet the Manager - As part of their monitoring and review processes, they have hosted Meet the Manager events where they were joined by Morgan Stanley (LCIV Global Equity Core Fund), Newton (LCIV Global Equity Fund), Longview (LCIV Global Equity Focus Fund), Ruffer (Absolute Return Fund) and The London LCIV itself.

c. There was a MTFS and budget presentation and discussion event held on the 12 November and the main points from that meetings follows:

- 2020/21 budget on track
- No proposal to change the Service charge or Development Funding Charge in 2021/22. So this will stay at £25k and £85k.
- Revised fee model will move to a 70% Ad Valorem/ 30% fixed fee basis but before the revised fee model can be implemented a target AUM of £17.5bn, (excluding passive) is required. Currently at £10bn.
- Pooling progress update – based on 31 March 2020 asset values there is potentially £17.5bn yet to be pooled.
- On assets pooled with LCIV, Havering is positioned in 6th place, falls into the classification of active investors with 70+% pooled, along with 8 other boroughs.

8.2.2 Review of the LCIV Funding Model and Cost Benchmarking

a. Ernst and Young (EY) who were appointed to undertake a review of the Funding Model have recommended remaining with the existing model until there is a critical level of Assets under Management (AUM), deemed to be at 75% of LGPS assets. The target AUM is £17.5bn, currently at £10bn.

b. Work has begun with EY to formally compare cross-pool costs but support from other pools has focused concerns about the level of detail and how the data will be used.

c. Discussion with other pools confirms that LCIV has a significant smaller budget even accounting for different pool activities such as in-house management.

8.2.3 Sub Fund Updates

a. Global Equity Core Fund – launched on the 19 October 2020.

b. Renewable Energy Fund – Stage 3 (Fund Structure Operational Viability stage). Having agreed the mandate with prospective Client Funds, they have issued and received back the Request for Proposals (RFPs) from interested parties within the adviser community, to assist London CIV in the forthcoming manager selection stage for each mandate. London CIV aiming to select the first manager for Renewable Infrastructure by late December which will lead to the fund launch in Q1 2021.

c. Impact Fund (aka London Fund - a partnership arrangement with the London Pension Fund Authority (LPFA) and Local Pensions Partnership (LPP)) – Fund launched on 15 December 2020 with a £150m investment. Second close expected in April 20201. So far two

London boroughs have expressed interest in this fund. Officers have been meeting with the LCIV to discuss this fund and have officer representation on the Seed Investor Group (SIG).

d. Private Debt – Stage 3 (Fund Structure Operational Viability stage) – Having agreed the mandate with prospective Client Funds, they have issued and received back the Request for Proposals (RFPs) from interested parties within the adviser community, to assist London CIV in the forthcoming manager selection stage for each mandate. Private Debt is anticipated to be launched in Q1 2021

e. Low Carbon mandate – new mandate being considered. Feedback was gathered from a survey that was issued in October 2020, which officers completed with the help of the Fund's investment Advisor. The SIG launched on the 4 November 2020 to discuss initial thoughts. Officers will joining the SIG for future meetings to have some input in how this mandate is developed.

f. Paris Aligned Global Equity Fund – This is a Paris aligned version of the Global Equity Fund managed by Baillie Gifford that LCIV are looking to launch in March 2021. This is in addition to the Baillie Gifford Global Equity Fund that Havering already invests in. Officers will liaise with the Fund's Investment Advisor and LCIV before discussing next steps with the Committee.

8.2.4 LCIV Key Staffing updates –

a. Three new members of staff joined the London CIV team. Tim Harris appointed to the Head of Operations and Tom Smith has been appointed as Assistant Manager for Compliance and Risk. Stephanie Aymes also appointed as their third Client Relations Manager.

b. London CIV announced the appointment of two new Non-Executive Directors - Alison Talbot and Kitty Ussher - who both joined the Board on Monday 21st September. Also appointed was Michael Green as a non-executive member of the Investment Oversight Committee.

8.3 LGPS GENERAL UPDATES:

8.3.1 Public sector exit payments

a. The statutory provisions governing exit payments to public sector workers (includes local government) are in the process of reform. This includes a £95k cap being applied for the total amount payable when someone exits their employment. The amount in severance payments, any pension strain cost (paid by the employer) and notice payments in excess of three months are included in the calculation.

b. The government initially published a consultation on 10 April 2019 seeking views on regulations implementing a £95,000 cap on exit payments in the public sector. The consultation closed on 3 July 2019.

c. On 21 July 2020, HM Treasury published the Governments response to the consultation and laid the implementing exit cap regulations in Parliament. These were approved by the House of Lords on 23 September and the House of Commons on 30 September. They were officially made on the 14 October 2020 and came into effect from 4 November 2020. This is in advance of the changes to LGPS regulations proposed by MHCLG in the further reform consultation (closing date of 9 November 2020 has been extended to the 18 December 2020).

d. There is a conflict between the exit cap regulations and the LGPS regulations. The LGPS regulations still require the member to take payment of an unreduced pension, but the exit cap regulations prevent the employer from paying the full strain cost. From 4 November 2020 up to the enactment of the regulations proposed by the MHCLG there is a position of legal uncertainty. It is expected that the LGPS regulations are not likely to come into force before March 2021

e. At the time of writing this report legal advice is being sought to determine the options available for the Fund and there are a number of judicial reviews in progress.

f. Actuarial advice has been received by the Fund in the options available for calculating the strain costs in becoming fit for purpose in the £95k cap environment and these will be included in the legal advice being sought.

8.3.2 LGPS Amendments to Statutory Underpin

LGPS Amendments to Statutory underpin consultation issued July 2020 with a deadline of 8 October 2020. This sets out how MHCLG proposes to remedy the McCloud age discrimination in the LGPS. Havering responded to the consultation and we await further updates.

8.3.3 Cost Cap

a. In 2014 the LGPS reformed to become a Career Average Revalued Earning Scheme (CARE). It was understood, at this time, that the cost of funding future pension benefits would be 19.5% of an employee’s salary. As a part of the reform, and to ensure the ongoing affordability of the LGPS, the Government introduced a ‘cost cap’ mechanism. This new mechanism involves checking the cost of LGPS pension provision every four years to ensure that these costs have not materially changed. In the event that the actual cost fell within 2% of 19.5%, no changes would be made to the Scheme's design.

b. The 2016 valuation showed that it cost less than 17.5% to fund future pension benefits, and so benefit improvements were expected to be made. However, due to the high profile court case the 'McCloud Judgment' has meant that the cost of funding pension provision has changed and this caused the cost cap mechanism to be paused.

c. An announcement was made in July 2020 that the 2016 Cost Cap process will now be 'unpaused' and the cost of resolving McCloud will now be included in the assessment of scheme costs. Accordingly, the government is preparing to complete the cost control element of the 2016 valuations. By taking into account the increased value of public service pensions as a result of 'McCloud remedy', scheme cost control valuation outcomes is expected to show greater costs than otherwise would have been expected. The government will consider how best to take forward the cost control mechanism outcomes for each scheme once the detail of these is known. We await further announcements.

8.3.4 Management of employer risk regulations

a. On 26 August MHCLG published its latest partial response to the May 2019 consultation called "Changes to the local valuation cycle and management of employer risk". The accompanying amendment regulations have also been made and are due to come into force from **23 September 2020**.

b. The new regulations focus on three key areas:
   - Review of employer contributions (inter- valuation)
   - Spreading exit debts
   - Deferred Debt Agreements

c. The Funding Strategy Statement will be amended to take account of these regulation changes and this item is also on the agenda for this meeting.

8.3.5 Good Governance in the LGPS

a. After delivering the Phase 2 report last year, the Scheme Advisory Board (SAB) asked Hymans to push forward with the working group and secretariat on more detailed implementation proposals. The project team updated the SAB at the meeting on **25th August 2020**.

b. Progress over recent months has been, understandably, a bit slower, as stakeholders have focussed on responding to immediate issues relating to the COVID-19 crisis. However, The SAB has re-iterated its commitment to this work and the project team will aim to have three key deliverables completed and agreed with the working group over the next month or so.

c. The project team agreed to progress 3 key deliverables, namely:

- A report setting out implementation advice for the proposals in Phase 2.
- A sample version of what a Fund's new Governance Compliance Statement (GCS) might look like including all the information in the proposals.
- A sample independent governance review report (IGR) which should help in developing procurement proposals for the independent governance review process.

d. The timetable thereafter will depend on the capacity within MHCLG and other LGPS stakeholders to progress to implementation of the proposals and consult on formal guidance given other priorities.

IMPLICATIONS AND RISKS

Financial implications and risks:

Pension Fund Managers' performances are regularly monitored in order to ensure that the investment objectives are being met and consequently minimise any cost to the General Fund and employers in the Fund

Legal implications and risks:

None arising directly from consideration of the content of the Report.

The Committee may be interested to note that LLG (Lawyers in Local Government) and ALACE (the Association of Local Authority Chief Executives and Senior Managers) have formally launched judicial review proceedings in a bid to quash the Exit Payment Cap Regulations. These proceedings are at an early stage and therefore it is not possible to provide any further detail.

The Committee has been constituted by the Council to perform the role of administering authority to manage the Havering LGPS Fund and as such has legal authority to consider and note the Report and presentations.

Human Resources implications and risks:

There are no immediate HR implications.

Equalities implications and risks:

The Public Sector Equality Duty (PSED) under section 149 of the Equality Act 2010 requires the Council, when exercising its functions, to have due regard to:

(i) The need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;

(ii) The need to advance equality of opportunity between persons who share protected characteristics and those who do not, and;

(iii) Foster good relations between those who have protected characteristics and those who do not.

Note: 'Protected characteristics' are: age, sex, race, disability, sexual orientation, marriage and civil partnerships, religion or belief, pregnancy and maternity and gender reassignment/identity.

The Council is committed to all of the above in the provision, procurement and commissioning of its services, and the employment of its workforce. In addition, the Council is also committed to improving the quality of life and wellbeing for all Havering residents in respect of socio-economics and health determinants.

An EqEIA is not considered necessary regarding this matter as the protected groups are not directly or indirectly affected

BACKGROUND PAPERS

None